Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 392.20 - Transportation Equipment - Trailers

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
1972	881.00	19.00	2.16%	-	0.00%	19.00	2.16%
1973	-	-	0.00%	-	0.00%	0.00	0.00%
1974	-	-	0.00%	-	0.00%	0.00	0.00%
1975	1,273.00	20.00	1.57%	-	0.00%	20.00	1.57%
1976	-	-	0.00%	-	0.00%	0.00	0.00%
1977	1,244.00	50.00	4.02%	-	0.00%	50.00	4.02%
1978	-	-	0.00%	-	0.00%	0.00	0.00%
1979	-	-	0.00%	-	0.00%	0.00	0.00%
1980	2,597.00	-	0.00%	-	0.00%	0.00	0.00%
1981	907.00	-	0.00%	-	0.00%	0.00	0.00%
1982	246.00	-	0.00%	-	0.00%	0.00	0.00%
1983	-	-	0.00%	-	0.00%	0.00	0.00%
1984	6,500.00	-	0.00%	-	0.00%	0.00	0.00%
1985	-	-	0.00%	-	0.00%	0.00	0.00%
1986	-	-	0.00%	-	0.00%	0.00	0.00%
1987	404.00	-	0.00%	-	0.00%	0.00	0.00%
1988	4,342.00	-	0.00%	-	0.00%	0.00	0.00%
1989	10,269.00	2,111.00	20.56%	-	0.00%	2,111.00	20.56%
1990	-	-	0.00%	-	0.00%	0.00	0.00%
1991	15,794.00	1,490.00	9.43%	-	0.00%	1,490.00	9.43%
1992	3,338.00	-	0.00%	-	0.00%	0.00	0.00%
1993	431.00	-	0.00%	-	0.00%	0.00	0.00%
1994	128,910.00	78,304.00	60.74%	304.00	0.24%	78,000.00	60.51%
1995	-	-	0.00%	-	0.00%	0.00	0.00%
1996	-	-	0.00%	-	0.00%	0.00	0.00%
1997	-	-	0.00%	-	0.00%	0.00	0.00%
1998	-	-	0.00%	-	0.00%	0.00	0.00%
1999	-	-	0.00%	-	0.00%	0.00	0.00%
2000	-	-	0.00%	-	0.00%	0.00	0.00%
2001	-	-	0.00%	-	0.00%	0.00	0.00%
2002	-	-	0.00%	-	0.00%	0.00	0.00%

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 392.20 - Transportation Equipment - Trailers

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
THREE - YEAR ROLLING BANDS							
1972-1974	881.00	19.00	2.16%	0.00	0.00%	19.00	2.16%
1973-1975	1,273.00	20.00	1.57%	0.00	0.00%	20.00	1.57%
1974-1976	1,273.00	20.00	1.57%	0.00	0.00%	20.00	1.57%
1975-1977	2,517.00	70.00	2.78%	0.00	0.00%	70.00	2.78%
1976-1978	1,244.00	50.00	4.02%	0.00	0.00%	50.00	4.02%
1977-1979	1,244.00	50.00	4.02%	0.00	0.00%	50.00	4.02%
1978-1980	2,597.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1979-1981	3,504.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1980-1982	3,750.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1981-1983	1,153.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1982-1984	6,746.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1983-1985	6,500.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1984-1986	6,500.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1985-1987	404.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1986-1988	4,746.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1987-1989	15,015.00	2,111.00	14.06%	0.00	0.00%	2,111.00	14.06%
1988-1990	14,611.00	2,111.00	14.45%	0.00	0.00%	2,111.00	14.45%
1989-1991	26,063.00	3,601.00	13.82%	0.00	0.00%	3,601.00	13.82%
1990-1992	19,132.00	1,490.00	7.79%	0.00	0.00%	1,490.00	7.79%
1991-1993	19,563.00	1,490.00	7.62%	0.00	0.00%	1,490.00	7.62%
1992-1994	132,679.00	78,304.00	59.02%	304.00	0.23%	78,000.00	58.79%
1993-1995	129,341.00	78,304.00	60.54%	304.00	0.24%	78,000.00	60.31%
1994-1996	128,910.00	78,304.00	60.74%	304.00	0.24%	78,000.00	60.51%
1995-1997	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1996-1998	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1997-1999	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1998-2000	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1999-2001	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
2000-2002	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1972-2002	177,136.00	81,994.00	46.29%	304.00	0.17%	81,690.00	46.12%

Trend Analysis (End Year) 2002

***Based Upon 3-Year Rolling Averages**

Annual Inflation	2.75%
ASL	25
Avg Ret Age	12.5
Years to ASL	12.5
Inflation Factor At 2.75% to ASL	1.40

Gross Salv. Trend Analysis*		
1983-2002	20-Year Trend	17.37%
1988-2002	15-Year Trend	8.76%
1993-2002	10-Year Trend	-13.43%
1998-2002	5-Year Trend	0.00%

Adjusted Salvage & C/O/R	**0.00%**	**0.24%**	**-0.24%**

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 393 - Stores Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
1972	-	-	0.00%	-		0.00	0.00%
1973	347.00	-	0.00%	-		0.00	0.00%
1974	-	-	0.00%	-		0.00	0.00%
1975	-	-	0.00%	-		0.00	0.00%
1976	-	-	0.00%	-		0.00	0.00%
1977	-	-	0.00%	-		0.00	0.00%
1978	14,182.00	200.00	1.41%	-		200.00	1.41%
1979	182.00	-	0.00%	-		0.00	0.00%
1980	-	-	0.00%	-		0.00	0.00%
1981	2,253.00	-	0.00%	94.00		(94.00)	-4.17%
1982	-	-	0.00%	-		0.00	0.00%
1983	-	-	0.00%	-		0.00	0.00%
1984	1,319.00	-	0.00%	-		0.00	0.00%
1985	789.00	-	0.00%	-		0.00	0.00%
1986	3,471.00	-	0.00%	91.00		(91.00)	-2.62%
1987	17,005.00	-	0.00%	-		0.00	0.00%
1988	-	-	0.00%	-		0.00	0.00%
1989	-	-	0.00%	-		0.00	0.00%
1990	-	-	0.00%	-		0.00	0.00%
1991	-	-	0.00%	-		0.00	0.00%
1992	-	-	0.00%	-		0.00	0.00%
1993	7,909.00	-	0.00%	-		0.00	0.00%
1994	-	-	0.00%	-		0.00	0.00%
1995	25,981.00	-	0.00%	46.00		(46.00)	-0.18%
1996	4,526.00	5,845.00	129.14%	-		5,845.00	129.14%
1997	969.00	2.00	0.21%	82.00		(80.00)	-8.26%
1998	-	-	0.00%	-		0.00	0.00%
1999	-	-	0.00%	-		0.00	0.00%
2000	-	-	0.00%	-		0.00	0.00%
2001	-	-	0.00%	-		0.00	0.00%
2002	8,778.00	-	0.00%	-		0.00	0.00%

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 393 - Stores Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
THREE - YEAR ROLLING BANDS							
1972-1974	347.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1973-1975	347.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1974-1976	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1975-1977	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1976-1978	14,182.00	200.00	1.41%	0.00	0.00%	200.00	1.41%
1977-1979	14,364.00	200.00	1.39%	0.00	0.00%	200.00	1.39%
1978-1980	14,364.00	200.00	1.39%	0.00	0.00%	200.00	1.39%
1979-1981	2,435.00	0.00	0.00%	94.00	3.86%	(94.00)	-3.86%
1980-1982	2,253.00	0.00	0.00%	94.00	4.17%	(94.00)	-4.17%
1981-1983	2,253.00	0.00	0.00%	94.00	4.17%	(94.00)	-4.17%
1982-1984	1,319.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1983-1985	2,108.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1984-1986	5,579.00	0.00	0.00%	91.00	1.63%	(91.00)	-1.63%
1985-1987	21,265.00	0.00	0.00%	91.00	0.43%	(91.00)	-0.43%
1986-1988	20,476.00	0.00	0.00%	91.00	0.44%	(91.00)	-0.44%
1987-1989	17,005.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1988-1990	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1989-1991	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1990-1992	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1991-1993	7,909.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1992-1994	7,909.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1993-1995	33,890.00	0.00	0.00%	46.00	0.14%	(46.00)	-0.14%
1994-1996	30,507.00	5,845.00	19.16%	46.00	0.15%	5,799.00	19.01%
1995-1997	31,476.00	5,847.00	18.58%	128.00	0.41%	5,719.00	18.17%
1996-1998	5,495.00	5,847.00	106.41%	82.00	1.49%	5,765.00	104.91%
1997-1999	969.00	2.00	0.21%	82.00	8.46%	(80.00)	-8.26%
1998-2000	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1999-2001	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
2000-2002	8,778.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1972-2002	87,711.00	6,047.00	6.89%	313.00	0.36%	5,734.00	6.54%

Trend Analysis (End Year) 2002

***Based Upon 3-Year Rolling Averages**

Annual Inflation	2.75%
ASL	33
Avg Ret Age	30.9
Years to ASL	2.1
Inflation Factor At 2.75% to ASL	1.06

Gross Salv. Trend Analysis*		
1983-2002	20-Year Trend	18.86%
1988-2002	15-Year Trend	20.38%
1993-2002	10-Year Trend	15.47%
1998-2002	5-Year Trend	-42.58%

Adjusted Salvage & C/O/R	**-42.58%**	**0.38%**	**-42.96%**

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 394 - Tools, Shop and Garage Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
1972	877.00	-	0.00%	-	0.00%	0.00	0.00%
1973	2,558.00	-	0.00%	-	0.00%	0.00	0.00%
1974	4,575.00	65.00	1.42%	-	0.00%	65.00	1.42%
1975	2,024.00	-	0.00%	-	0.00%	0.00	0.00%
1976	8,833.00	-	0.00%	-	0.00%	0.00	0.00%
1977	6,490.00	642.00	9.89%	2.00	0.03%	640.00	9.86%
1978	1,730.00	-	0.00%	-	0.00%	0.00	0.00%
1979	3,156.00	-	0.00%	-	0.00%	0.00	0.00%
1980	4,310.00	-	0.00%	-	0.00%	0.00	0.00%
1981	4,262.00	-	0.00%	-	0.00%	0.00	0.00%
1982	650.00	25.00	3.85%	-	0.00%	25.00	3.85%
1983	147.00	94.00	63.95%	-	0.00%	94.00	63.95%
1984	2,200.00	450.00	20.45%	-	0.00%	450.00	20.45%
1985	5,408.00	150.00	2.77%	-	0.00%	150.00	2.77%
1986	3,252.00	-	0.00%	15.00	0.46%	(15.00)	-0.46%
1987	2,628.00	62.00	2.36%	-	0.00%	62.00	2.36%
1988	2,163.00	52.00	2.40%	-	0.00%	52.00	2.40%
1989	15,597.00	4,142.00	26.56%	61,113.00	391.83%	(56,971.00)	-365.27%
1990	-	-	0.00%	-	0.00%	0.00	0.00%
1991	565.00	-	0.00%	-	0.00%	0.00	0.00%
1992	74,622.00	9,493.00	12.72%	-	0.00%	9,493.00	12.72%
1993	-	-	0.00%	-	0.00%	0.00	0.00%
1994	561,980.00	108,578.00	19.32%	8,912.00	1.59%	99,666.00	17.73%
1995	7,086.00	-	0.00%	12.00	0.17%	(12.00)	-0.17%
1996	-	-	0.00%	-	0.00%	0.00	0.00%
1997	-	-	0.00%	-	0.00%	0.00	0.00%
1998	-	-	0.00%	-	0.00%	0.00	0.00%
1999	-	-	0.00%	-	0.00%	0.00	0.00%
2000	10,759.00	662.00	6.15%	(570.00)	-5.30%	1,232.00	11.45%
2001	-	-	0.00%	-	0.00%	0.00	0.00%
2002	718.00	-	0.00%	-	0.00%	0.00	0.00%

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 394 - Tools, Shop and Garage Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
THREE - YEAR ROLLING BANDS							
1972-1974	8,010.00	65.00	0.81%	0.00	0.00%	65.00	0.81%
1973-1975	9,157.00	65.00	0.71%	0.00	0.00%	65.00	0.71%
1974-1976	15,432.00	65.00	0.42%	0.00	0.00%	65.00	0.42%
1975-1977	17,347.00	642.00	3.70%	2.00	0.01%	640.00	3.69%
1976-1978	17,053.00	642.00	3.76%	2.00	0.01%	640.00	3.75%
1977-1979	11,376.00	642.00	5.64%	2.00	0.02%	640.00	5.63%
1978-1980	9,196.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1979-1981	11,728.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1980-1982	9,222.00	25.00	0.27%	0.00	0.00%	25.00	0.27%
1981-1983	5,059.00	119.00	2.35%	0.00	0.00%	119.00	2.35%
1982-1984	2,997.00	569.00	18.99%	0.00	0.00%	569.00	18.99%
1983-1985	7,755.00	694.00	8.95%	0.00	0.00%	694.00	8.95%
1984-1986	10,860.00	600.00	5.52%	15.00	0.14%	585.00	5.39%
1985-1987	11,288.00	212.00	1.88%	15.00	0.13%	197.00	1.75%
1986-1988	8,043.00	114.00	1.42%	15.00	0.19%	99.00	1.23%
1987-1989	20,388.00	4,256.00	20.88%	61,113.00	299.75%	(56,857.00)	-278.87%
1988-1990	17,760.00	4,194.00	23.61%	61,113.00	344.10%	(56,919.00)	-320.49%
1989-1991	16,162.00	4,142.00	25.63%	61,113.00	378.13%	(56,971.00)	-352.50%
1990-1992	75,187.00	9,493.00	12.63%	0.00	0.00%	9,493.00	12.63%
1991-1993	75,187.00	9,493.00	12.63%	0.00	0.00%	9,493.00	12.63%
1992-1994	636,602.00	118,071.00	18.55%	8,912.00	1.40%	109,159.00	17.15%
1993-1995	569,066.00	108,578.00	19.08%	8,924.00	1.57%	99,654.00	17.51%
1994-1996	569,066.00	108,578.00	19.08%	8,924.00	1.57%	99,654.00	17.51%
1995-1997	7,086.00	0.00	0.00%	12.00	0.17%	(12.00)	-0.17%
1996-1998	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1997-1999	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1998-2000	10,759.00	662.00	6.15%	(570.00)	-5.30%	1,232.00	11.45%
1999-2001	10,759.00	662.00	6.15%	(570.00)	-5.30%	1,232.00	11.45%
2000-2002	11,477.00	662.00	5.77%	(570.00)	-4.97%	1,232.00	10.73%
1972-2002	726,590.00	124,415.00	17.12%	69,484.00	9.56%	54,931.00	7.56%

Trend Analysis (End Year) 2002

***Based Upon 3-Year Rolling Averages**

Annual Inflation	2.75%
ASL	20
Avg Ret Age	16.8
Years to ASL	3.2
Inflation Factor At 2.75% to ASL	1.09

Gross Salv. Trend Analysis*		
1983-2002	20-Year Trend	7.65%
1988-2002	15-Year Trend	2.57%
1993-2002	10-Year Trend	-0.27%
1998-2002	5-Year Trend	8.92%

Adjusted Salvage & C/O/R	**8.92%**	**10.43%**	**-1.51%**

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 395 - Laboratory Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
1972	58.00	3.00			0.00%	3.00	5.17%
1973	-	-	0.00%	-	0.00%	0.00	0.00%
1974	6,754.00	3,408.00			0.00%	3,408.00	50.46%
1975	-	-	0.00%	-	0.00%	0.00	0.00%
1976	-	-	0.00%	-	0.00%	0.00	0.00%
1977	-	-	0.00%	-	0.00%	0.00	0.00%
1978	-	-	0.00%	-	0.00%	0.00	0.00%
1979	-	-	0.00%	-	0.00%	0.00	0.00%
1980	-	-	0.00%	-	0.00%	0.00	0.00%
1981	-	-	0.00%	-	0.00%	0.00	0.00%
1982	-	-	0.00%	-	0.00%	0.00	0.00%
1983	-	-	0.00%	-	0.00%	0.00	0.00%
1984	-	-	0.00%	-	0.00%	0.00	0.00%
1985	-	-	0.00%	-	0.00%	0.00	0.00%
1986	-	-	0.00%	-	0.00%	0.00	0.00%
1987	-	-	0.00%	-	0.00%	0.00	0.00%
1988	-	-	0.00%	-	0.00%	0.00	0.00%
1989	-	-	0.00%	-	0.00%	0.00	0.00%
1990	-	-	0.00%	-	0.00%	0.00	0.00%
1991	-	-	0.00%	-	0.00%	0.00	0.00%
1992	-	-	0.00%	-	0.00%	0.00	0.00%
1993	-	-	0.00%	-	0.00%	0.00	0.00%
1994	24,958.00	4,822.00		396.00	1.59%	4,426.00	17.73%
1995	-	-	0.00%	-	0.00%	0.00	0.00%
1996	-	-	0.00%	-	0.00%	0.00	0.00%
1997	-	-	0.00%	-	0.00%	0.00	0.00%
1998	-	-	0.00%	-	0.00%	0.00	0.00%
1999	-	-	0.00%	-	0.00%	0.00	0.00%
2000	-	-	0.00%	-	0.00%	0.00	0.00%
2001	-	-	0.00%	-	0.00%	0.00	0.00%
2002	-	-	0.00%	-	0.00%	0.00	0.00%

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 395 - Laboratory Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
THREE - YEAR ROLLING BANDS							
1972-1974	6,812.00	3,411.00	50.07%	0.00	0.00%	3,411.00	50.07%
1973-1975	6,754.00	3,408.00	50.46%	0.00	0.00%	3,408.00	50.46%
1974-1976	6,754.00	3,408.00	50.46%	0.00	0.00%	3,408.00	50.46%
1975-1977	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1976-1978	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1977-1979	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1978-1980	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1979-1981	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1980-1982	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1981-1983	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1982-1984	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1983-1985	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1984-1986	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1985-1987	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1986-1988	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1987-1989	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1988-1990	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1989-1991	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1990-1992	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1991-1993	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1992-1994	24,958.00	4,822.00	19.32%	396.00	1.59%	4,426.00	17.73%
1993-1995	24,958.00	4,822.00	19.32%	396.00	1.59%	4,426.00	17.73%
1994-1996	24,958.00	4,822.00	19.32%	396.00	1.59%	4,426.00	17.73%
1995-1997	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1996-1998	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1997-1999	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1998-2000	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1999-2001	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
2000-2002	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1972-2002	31,770.00	8,233.00	25.91%	396.00	1.25%	7,837.00	24.67%

Trend Analysis (End Year) 2002

***Based Upon 3-Year Rolling Averages**

Annual Inflation	2.75%
ASL	18
Avg Ret Age	20.3
Years to ASL	-2.3
Inflation Factor At 2.75% to ASL	0.94

Gross Salv. Trend Analysis*		
1983-2002	20-Year Trend	5.19%
1988-2002	15-Year Trend	3.86%
1993-2002	10-Year Trend	-3.86%
1998-2002	5-Year Trend	0.00%

Adjusted Salvage & C/O/R	**0.00%**	**1.17%**	**-1.17%**

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 396.20 - Power Operated Equipment - Other

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
1972	1,035.00	-	0.00%	-	0.00%	0.00	0.00%
1973	6,725.00	-	0.00%	-	0.00%	0.00	0.00%
1974	1,147.00	-	0.00%	-	0.00%	0.00	0.00%
1975	50.00	-	0.00%	-	0.00%	0.00	0.00%
1976	748.00	1,000.00	133.69%	-	0.00%	1,000.00	133.69%
1977	745.00	-	0.00%	-	0.00%	0.00	0.00%
1978	473.00	-	0.00%	-	0.00%	0.00	0.00%
1979	-	-	0.00%	-	0.00%	0.00	0.00%
1980	50.00	-	0.00%	-	0.00%	0.00	0.00%
1981	7,271.00	1,500.00	20.63%	-	0.00%	1,500.00	20.63%
1982	-	-	0.00%	-	0.00%	0.00	0.00%
1983	-	-	0.00%	-	0.00%	0.00	0.00%
1984	-	-	0.00%	-	0.00%	0.00	0.00%
1985	648.00	-	0.00%	-	0.00%	0.00	0.00%
1986	-	-	0.00%	-	0.00%	0.00	0.00%
1987	200.00	-	0.00%	-	0.00%	0.00	0.00%
1988	257.00	125.00	48.64%	-	0.00%	125.00	48.64%
1989	1,574.00	841.00	53.43%	-	0.00%	841.00	53.43%
1990	-	-	0.00%	-	0.00%	0.00	0.00%
1991	-	-	0.00%	-	0.00%	0.00	0.00%
1992	100.00	778.00	778.00%	-	0.00%	778.00	778.00%
1993	-	-	0.00%	-	0.00%	0.00	0.00%
1994	370,828.00	71,646.00	19.32%	5,881.00	1.59%	65,765.00	17.73%
1995	-	-	0.00%	-	0.00%	0.00	0.00%
1996	-	-	0.00%	-	0.00%	0.00	0.00%
1997	-	-	0.00%	-	0.00%	0.00	0.00%
1998	-	-	0.00%	-	0.00%	0.00	0.00%
1999	-	-	0.00%	-	0.00%	0.00	0.00%
2000	-	-	0.00%	-	0.00%	0.00	0.00%
2001	-	-	0.00%	-	0.00%	0.00	0.00%
2002	2,196.00	-	0.00%	-	0.00%	0.00	0.00%

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 396.20 - Power Operated Equipment - Other

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
THREE - YEAR ROLLING BANDS							
1972-1974	8,907.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1973-1975	7,922.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1974-1976	1,945.00	1,000.00	51.41%	0.00	0.00%	1,000.00	51.41%
1975-1977	1,543.00	1,000.00	64.81%	0.00	0.00%	1,000.00	64.81%
1976-1978	1,966.00	1,000.00	50.86%	0.00	0.00%	1,000.00	50.86%
1977-1979	1,218.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1978-1980	523.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1979-1981	7,321.00	1,500.00	20.49%	0.00	0.00%	1,500.00	20.49%
1980-1982	7,321.00	1,500.00	20.49%	0.00	0.00%	1,500.00	20.49%
1981-1983	7,271.00	1,500.00	20.63%	0.00	0.00%	1,500.00	20.63%
1982-1984	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1983-1985	648.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1984-1986	648.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1985-1987	848.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1986-1988	457.00	125.00	27.35%	0.00	0.00%	125.00	27.35%
1987-1989	2,031.00	966.00	47.56%	0.00	0.00%	966.00	47.56%
1988-1990	1,831.00	966.00	52.76%	0.00	0.00%	966.00	52.76%
1989-1991	1,574.00	841.00	53.43%	0.00	0.00%	841.00	53.43%
1990-1992	100.00	778.00	778.00%	0.00	0.00%	778.00	778.00%
1991-1993	100.00	778.00	778.00%	0.00	0.00%	778.00	778.00%
1992-1994	370,928.00	72,424.00	19.53%	5,881.00	1.59%	66,543.00	17.94%
1993-1995	370,828.00	71,646.00	19.32%	5,881.00	1.59%	65,765.00	17.73%
1994-1996	370,828.00	71,646.00	19.32%	5,881.00	1.59%	65,765.00	17.73%
1995-1997	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1996-1998	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1997-1999	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1998-2000	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1999-2001	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
2000-2002	2,196.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1972-2002	394,047.00	75,890.00	19.26%	5,881.00	1.49%	70,009.00	17.77%

Trend Analysis (End Year) 2002

***Based Upon 3-Year Rolling Averages**

Annual Inflation	2.75%
ASL	23
Avg Ret Age	24.9
Years to ASL	-1.9
Inflation Factor At 2.75% to ASL	0.95

Gross Salv. Trend Analysis*		
1983-2002	20-Year Trend	82.07%
1988-2002	15-Year Trend	-18.73%
1993-2002	10-Year Trend	-159.49%
1998-2002	5-Year Trend	0.00%

Adjusted Salvage & C/O/R	**0.00%**	**1.42%**	**-1.42%**

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 397 - Communication Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
1972	72.00	5.00	6.94%		0.00%	5.00	6.94%
1973	13,492.00	5,912.00	43.82%	831.00	6.16%	5,081.00	37.66%
1974	9,357.00	5,952.00	63.61%	741.00	7.92%	5,211.00	55.69%
1975	106,938.00	11,278.00	10.55%	1,551.00	1.45%	9,727.00	9.10%
1976	52,136.00	30,203.00	57.93%	7,259.00	13.92%	22,944.00	44.01%
1977	55,509.00	18,438.00	33.22%	11,245.00	20.26%	7,193.00	12.96%
1978	13,986.00	1,487.00	10.63%	835.00	5.97%	652.00	4.66%
1979	38,007.00	3,829.00	10.07%	2,467.00	6.49%	1,362.00	3.58%
1980	13,375.00	858.00	6.41%	1,003.00	7.50%	(145.00)	-1.08%
1981	72,145.00	11,702.00	16.22%	858.00	1.19%	10,844.00	15.03%
1982	253,234.00	62,034.00	24.50%	1,563.00	0.62%	60,471.00	23.88%
1983	19,461.00	719.00	3.69%	4,127.00	21.21%	(3,408.00)	-17.51%
1984	40,780.00	4,231.00	10.38%	6,936.00	17.01%	(2,705.00)	-6.63%
1985	50,961.00	2,354.00	4.62%	5,378.00	10.55%	(3,024.00)	-5.93%
1986	70,934.00	772.00	1.09%	5,416.00	7.64%	(4,644.00)	-6.55%
1987	27,034.00	181.00	0.67%	2,536.00	9.38%	(2,355.00)	-8.71%
1988	33,348.00	578.00	1.73%	2,420.00	7.26%	(1,842.00)	-5.52%
1989	44,524.00	4,140.00	9.30%	10,469.00	23.51%	(6,329.00)	-14.21%
1990	157,605.00		0.00%	5,806.00	3.68%	(5,806.00)	-3.68%
1991	60,019.00	2,351.00	3.92%	(474.00)	-0.79%	2,825.00	4.71%
1992	51,909.00	1,954.00	3.76%	4,843.00	9.33%	(2,889.00)	-5.57%
1993	64,042.00	-	0.00%	2,666.00	4.16%	(2,666.00)	-4.16%
1994	43,479.00	458.00	1.05%	1,452.00	3.34%	(994.00)	-2.29%
1995	1,667,024.00	281.00	0.02%	21,942.00	1.32%	(21,661.00)	-1.30%
1996	808,552.00	-	0.00%	5,046.00	0.62%	(5,046.00)	-0.62%
1997	638,377.00	1,167.00	0.18%	53,732.00	8.42%	(52,565.00)	-8.23%
1998	105,064.00	6,993.00	6.66%	(114,380.00)	-108.87%	121,373.00	115.52%
1999	284,763.00	(12,179.00)	-4.28%	186,148.00	65.37%	(198,327.00)	-69.65%
2000	14,328.00	-	0.00%	-	0.00%	0.00	0.00%
2001	-	-	0.00%	-	0.00%	0.00	0.00%
2002	7,983.00	-	0.00%	-	0.00%	0.00	0.00%

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 397 - Communication Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
THREE - YEAR ROLLING BANDS							
1972-1974	22,921.00	11,869.00	51.78%	1,572.00	6.86%	10,297.00	44.92%
1973-1975	129,787.00	23,142.00	17.83%	3,123.00	2.41%	20,019.00	15.42%
1974-1976	168,431.00	47,433.00	28.16%	9,551.00	5.67%	37,882.00	22.49%
1975-1977	214,583.00	59,919.00	27.92%	20,055.00	9.35%	39,864.00	18.58%
1976-1978	121,631.00	50,128.00	41.21%	19,339.00	15.90%	30,789.00	25.31%
1977-1979	107,502.00	23,754.00	22.10%	14,547.00	13.53%	9,207.00	8.56%
1978-1980	65,368.00	6,174.00	9.44%	4,305.00	6.59%	1,869.00	2.86%
1979-1981	123,527.00	16,389.00	13.27%	4,328.00	3.50%	12,061.00	9.76%
1980-1982	338,754.00	74,594.00	22.02%	3,424.00	1.01%	71,170.00	21.01%
1981-1983	344,840.00	74,455.00	21.59%	6,548.00	1.90%	67,907.00	19.69%
1982-1984	313,475.00	66,984.00	21.37%	12,626.00	4.03%	54,358.00	17.34%
1983-1985	111,202.00	7,304.00	6.57%	16,441.00	14.78%	(9,137.00)	-8.22%
1984-1986	162,675.00	7,357.00	4.52%	17,730.00	10.90%	(10,373.00)	-6.38%
1985-1987	148,929.00	3,307.00	2.22%	13,330.00	8.95%	(10,023.00)	-6.73%
1986-1988	131,316.00	1,531.00	1.17%	10,372.00	7.90%	(8,841.00)	-6.73%
1987-1989	104,906.00	4,899.00	4.67%	15,425.00	14.70%	(10,526.00)	-10.03%
1988-1990	235,477.00	4,718.00	2.00%	18,695.00	7.94%	(13,977.00)	-5.94%
1989-1991	262,148.00	6,491.00	2.48%	15,801.00	6.03%	(9,310.00)	-3.55%
1990-1992	269,533.00	4,305.00	1.60%	10,175.00	3.78%	(5,870.00)	-2.18%
1991-1993	175,970.00	4,305.00	2.45%	7,035.00	4.00%	(2,730.00)	-1.55%
1992-1994	159,430.00	2,412.00	1.51%	8,961.00	5.62%	(6,549.00)	-4.11%
1993-1995	1,774,545.00	739.00	0.04%	26,060.00	1.47%	(25,321.00)	-1.43%
1994-1996	2,519,055.00	739.00	0.03%	28,440.00	1.13%	(27,701.00)	-1.10%
1995-1997	3,113,953.00	1,448.00	0.05%	80,720.00	2.59%	(79,272.00)	-2.55%
1996-1998	1,551,993.00	8,160.00	0.53%	(55,602.00)	-3.58%	63,762.00	4.11%
1997-1999	1,028,204.00	-4,019.00	-0.39%	125,500.00	12.21%	(129,519.00)	-12.60%
1998-2000	404,155.00	-5,186.00	-1.28%	71,768.00	17.76%	(76,954.00)	-19.04%
1999-2001	299,091.00	-12,179.00	-4.07%	186,148.00	62.24%	(198,327.00)	-66.31%
2000-2002	22,311.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1972-2002	4,818,438.00	165,698.00	3.44%	232,416.00	4.82%	-66,718.00	-1.38%

Trend Analysis (End Year) 2002

***Based Upon 3-Year Rolling Averages**

Annual Inflation	2.75%
ASL	15
Avg Ret Age	11.5
Years to ASL	3.5
Inflation Factor At 2.75% to ASL	1.10

Gross Salv. Trend Analysis*		
1983-2002	20-Year Trend	-5.31%
1988-2002	15-Year Trend	-2.08%
1993-2002	10-Year Trend	-2.40%
1998-2002	5-Year Trend	-2.46%

Adjusted Salvage & C/O/R	**-2.46%**	**5.30%**	**-7.77%**

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 398 - Miscellaneous Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
1972	-	-	0.00%	-	0.00%	0.00	0.00%
1973	-	-	0.00%	-	0.00%	0.00	0.00%
1974	-	-	0.00%	-	0.00%	0.00	0.00%
1975	-	-	0.00%	-	0.00%	0.00	0.00%
1976	-	-	0.00%	-	0.00%	0.00	0.00%
1977	-	-	0.00%	-	0.00%	0.00	0.00%
1978	-	-	0.00%	-	0.00%	0.00	0.00%
1979	-	-	0.00%	-	0.00%	0.00	0.00%
1980	-	-	0.00%	-	0.00%	0.00	0.00%
1981	-	-	0.00%	-	0.00%	0.00	0.00%
1982	-	-	0.00%	-	0.00%	0.00	0.00%
1983	-	-	0.00%	-	0.00%	0.00	0.00%
1984	-	-	0.00%	-	0.00%	0.00	0.00%
1985	-	-	0.00%	-	0.00%	0.00	0.00%
1986	-	-	0.00%	-	0.00%	0.00	0.00%
1987	2,529.00	-	0.00%	-	0.00%	0.00	0.00%
1988	-	-	0.00%	-	0.00%	0.00	0.00%
1989	-	-	0.00%	-	0.00%	0.00	0.00%
1990	-	-	0.00%	-	0.00%	0.00	0.00%
1991	-	-	0.00%	-	0.00%	0.00	0.00%
1992	-	-	0.00%	-	0.00%	0.00	0.00%
1993	-	-	0.00%	-	0.00%	0.00	0.00%
1994	-	-	0.00%	-	0.00%	0.00	0.00%
1995	-	-	0.00%	-	0.00%	0.00	0.00%
1996	-	-	0.00%	-	0.00%	0.00	0.00%
1997	-	-	0.00%	-	0.00%	0.00	0.00%
1998	-	-	0.00%	-	0.00%	0.00	0.00%
1999	-	-	0.00%	-	0.00%	0.00	0.00%
2000	-	-	0.00%	-	0.00%	0.00	0.00%
2001	-	-	0.00%	-	0.00%	0.00	0.00%
2002	-	-	0.00%	-	0.00%	0.00	0.00%

Louisville Gas and Electric
Common Plant

Analysis of Experienced Salvage
1972 through 2002

Account 398 - Miscellaneous Equipment

Year	Original Cost of Retirements	Gross Salvage	%	Cost of Removal	%	Net Salvage	%
THREE - YEAR ROLLING BANDS							
1972-1974	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1973-1975	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1974-1976	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1975-1977	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1976-1978	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1977-1979	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1978-1980	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1979-1981	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1980-1982	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1981-1983	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1982-1984	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1983-1985	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1984-1986	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1985-1987	2,529.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1986-1988	2,529.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1987-1989	2,529.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1988-1990	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1989-1991	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1990-1992	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1991-1993	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1992-1994	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1993-1995	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1994-1996	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1995-1997	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1996-1998	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1997-1999	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1998-2000	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1999-2001	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
2000-2002	0.00	0.00	0.00%	0.00	0.00%	0.00	0.00%
1972-2002	2,529.00	0.00	0.00%	0.00	0.00%	0.00	0.00%

Trend Analysis (End Year) 2002

***Based Upon 3-Year Rolling Averages**

Annual Inflation	2.75%
ASL	20
Avg Ret Age	1.5
Years to ASL	18.5
Inflation Factor At 2.75% to ASL	1.65

Gross Salv. Trend Analysis*		
1983-2002	20-Year Trend	0.00%
1988-2002	15-Year Trend	0.00%
1993-2002	10-Year Trend	0.00%
1998-2002	5-Year Trend	0.00%

Adjusted Salvage & C/O/R	**0.00%**	**0.00%**	**0.00%**

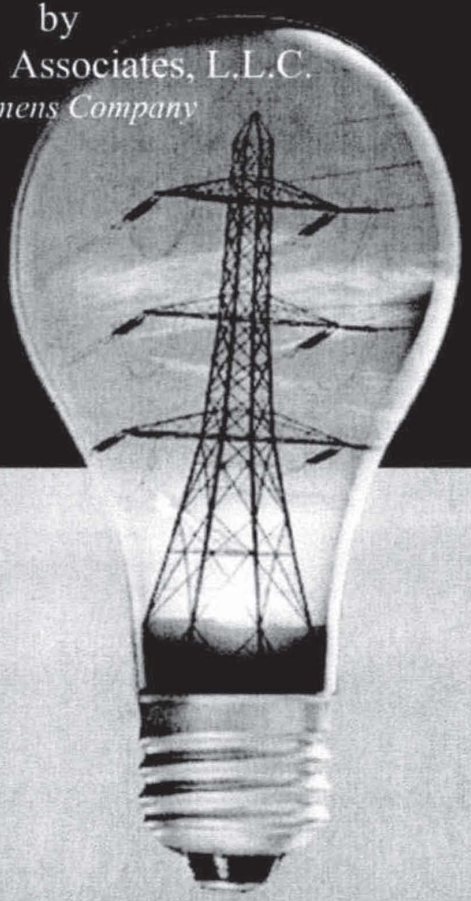
Attachment to Response to
LGE KIUC-2 Question No. 80

Attachment No. 3

An Economic Life Assessment of Generation Assets of KU and LG&E Performed for

e·on U.S.

E.ON U.S.
by
NewEnergy Associates, L.L.C.
A Siemens Company



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A Siemens Company

NewEnergy ASSOCIATES
A Siemens Company

Suite 1500 • 400 Interstate North Parkway • Atlanta, Georgia 30339 • 770.779.2800 • www.newenergyassoc.com

Table of Contents

A. Introduction:

In order to determine the effective useful economic life of E.ON U.S.'s generating assets, NewEnergy Associates, LLC was retained by E.ON U.S. to perform a Life Assessment of its generating assets. The goal of the analysis was to allow E.ON U.S. to more accurately project when a generating asset will reach the end of its effective useful economic life. With the information supplied by NewEnergy Associates, E.ON U.S. will have a more robust method of determining the depreciation life of an asset. NewEnergy utilized its Strategist strategic planning model, together with E.ON U.S.'s data, to perform this analysis.

B. Methodology:

The analysis was conducted in two phases: an initial phase (Phase 1) to focus on a subset of the generating assets and demonstrate the effectiveness of the proposed methodology, and a second phase (Phase 2) to complete the analysis for the balance of generating assets. The specific tasks for each Phase of the analysis are shown in Appendix A.

For E.ON U.S.'s Life Assessment, units in service for less than 30 years were excluded from the evaluation. None of these units will have been in service for more than 60 years at the end of 2035 and current industry practice indicates that it is both reasonable and cost effective to retain properly operated and maintained units for a life of at least 60 years. The units excluded on the basis of this criterion were the E.W. Brown, Trimble County, Paddys Run 13 combustion turbines, and the Trimble County 1, Ghent 3 & 4, and Mill Creek 3 & 4 coal units.

Figure 1:

Retirement Candidates by Type:

	Net MW	
	Winter 2005	**Summer 2005**
Coal Steam	3,049	3,057
Hydro	56	72
CT	113	99
Total Capacity	**3,218**	**3,228**

Figure 1 shows the total MW of each capacity type of the KU and LG&E assets that were considered for the analysis. Figure 2 shows all KU and LG&E assets and shows the total capacity for those considered in the Life Assessment Analysis. These assets total 3,228 MW (summer). Highlighted assets were not considered in this assessment.

Figure 2:

Kentucky Utilities' Company / Louisville Gas and Electric Company

2006 Generator Ratings (MW)

Plant Name	Owner	In-Service Date	Net Winter 2005	Net Summer 2005	Unit Type	Fuel Type	Age as of December 31, 2006	Age as of December 31, 2035
Brown 1	KU	May 1, 1957	102	101	Steam	Coal	49.67	78.67
Brown 2	KU	June 1, 1963	169	167	Steam	Coal	43.58	72.58
Brown 3	KU	July 1, 1971	433	429	Steam	Coal	35.50	64.50
Total Brown Coal			**704**	**697**				
IAC on 11N2	KU	June 1, 2000		98	Inlet Air Cooling		6.58	35.58
Brown 5	Joint	June 8, 2001	143	117	CT	Natural Gas	5.56	34.56
Brown 6	Joint	August 11, 1999	168	154	CT	Natural Gas/Oil	7.39	36.39
Brown 7	Joint	August 8, 1999	168	154	CT	Natural Gas/Oil	7.40	36.40
Brown 8	KU	February 1, 1995	140	106	CT	Natural Gas/Oil	11.91	40.91
Brown 9	KU	August 1, 1994	140	106	CT	Natural Gas/Oil	12.42	41.42
Brown 10	KU	December 1, 1995	140	106	CT	Natural Gas/Oil	11.08	40.08
Brown 11	KU	May 1, 1996	140	106	CT	Natural Gas/Oil	10.67	39.67
Total Brown CT			**1,039**	**947**				
Cane Run 4	LGE	May 1, 1962	155	155	Steam	Coal	44.67	73.67
Cane Run 5	LGE	May 1, 1966	168	168	Steam	Coal	40.67	69.67
Cane Run 6	LGE	May 1, 1969	240	240	Steam	Coal	37.67	66.67
Total Cane Run			**563**	**563**				
Dix Dam 1	KU	November 1, 1925	8	8	Hydro	Water	81.16	110.16
Dix Dam 2	KU	November 1, 1925	8	8	Hydro	Water	81.16	110.16
Dix Dam 3	KU	November 1, 1925	8	8	Hydro	Water	81.16	110.16
Total Dix Dam			**24**	**24**				
Ghent 1	KU	February 1, 1974	468	475	Steam	Coal	32.91	61.91
Ghent 2	KU	April 1, 1977	466	484	Steam	Coal	29.75	58.75
Ghent 3	KU	May 1, 1981	495	493	Steam	Coal	25.67	54.67
Ghent 4	KU	August 1, 1984	495	493	Steam	Coal	22.41	51.41
Total Ghent			**1,924**	**1,945**				
Green River 3	KU	April 1, 1954	71	68	Steam	Coal	52.75	81.75
Green River 4	KU	July 1, 1959	102	95	Steam	Coal	47.50	76.50
Total Green River			**173**	**163**				
Haefling 1	KU	October 1, 1970	14	12	CT	Natural Gas/Oil	36.25	65.25
Haefling 2	KU	October 1, 1970	14	12	CT	Natural Gas/Oil	36.25	65.25
Haefling 3	KU	October 1, 1970	14	12	CT	Natural Gas/Oil	36.25	65.25
Total Haefling			**42**	**36**				
Mill Creek 1	LGE	August 1, 1972	303	303	Steam	Coal	34.41	63.41
Mill Creek 2	LGE	July 1, 1974	299	301	Steam	Coal	32.50	61.50
Mill Creek 3	LGE	August 1, 1978	397	391	Steam	Coal	28.42	57.42
Mill Creek 4	LGE	September 1, 1982	492	477	Steam	Coal	24.33	53.33
Total Mill Creek			**1,491**	**1,472**				
Ohio Falls 1	LGE	January 1, 1928	4	6	Hydro	Water	79.00	108.00
Ohio Falls 2	LGE	January 1, 1928	4	6	Hydro	Water	79.00	108.00
Ohio Falls 3	LGE	January 1, 1928	4	6	Hydro	Water	79.00	108.00
Ohio Falls 4	LGE	January 1, 1928	4	6	Hydro	Water	79.00	108.00
Ohio Falls 5	LGE	January 1, 1928	4	6	Hydro	Water	79.00	108.00
Ohio Falls 6	LGE	January 1, 1928	4	6	Hydro	Water	79.00	108.00
Ohio Falls 7	LGE	January 1, 1928	4	6	Hydro	Water	79.00	108.00
Ohio Falls 8	LGE	January 1, 1928	4	6	Hydro	Water	79.00	108.00
Total Ohio Falls Hydro			**32**	**48**				
Paddys Run 13	Joint	June 27, 2001	175	158	CT	Natural Gas	5.51	34.51
Total Paddys Run CT			**175**	**158**				
Trimble County 1	LGE	December 23, 1990	386	383	Steam	Coal	16.02	45.02
Total Trimble County			**386**	**383**				
Trimble County 5	Joint	May 14, 2002	180	160	CT	Natural Gas	4.63	33.63
Trimble County 6	Joint	May 14, 2002	180	160	CT	Natural Gas	4.63	33.63
Trimble County 7	Joint	June 1, 2004	180	160	CT	Natural Gas	2.58	31.58
Trimble County 8	Joint	June 1, 2004	180	160	CT	Natural Gas	2.58	31.58
Trimble County 9	Joint	July 1, 2004	180	160	CT	Natural Gas	2.50	31.50
Trimble County 10	Joint	July 1, 2004	180	160	CT	Natural Gas	2.50	31.50
Total Trimble County CT			**1,080**	**960**				
Tyrone 1	KU	October 1, 1947	30	27	CT	Oil	59.25	88.25
Tyrone 2	KU	June 1, 1948	33	31	CT	Oil	58.58	87.58
Tyrone 3	KU	July 1, 1953	73	71	Steam	Coal	53.50	82.50
Total Tyrone			**136**	**129**				
Cane Run 11	LGE	June 1, 1968	14	14	CT	Natural Gas/Oil	38.58	67.58
Paddy's Run 11	LGE	June 1, 1968	13	12	CT	Natural Gas	38.58	67.58
Paddy's Run 12	LGE	July 1, 1968	28	23	CT	Natural Gas	38.50	67.50
Waterside 7	LGE	June 1, 1964	13	11	CT	Natural Gas	42.58	71.58
Waterside 8	LGE	February 1, 1964	13	11	CT	Natural Gas	42.91	71.91
Zorn 1	LGE	May 1, 1969	16	14	CT	Natural Gas	37.67	66.67
Total LG&E CT's			**97**	**85**				
		Total Study Capacity	**3,218**	**3,228**		**Weighted age**	**38**	**67**
							Winter MW	**Summer MW**
	Units that will be less than 60 yrs old in 2035 were not considered in the study.						4,559	4,302
	Units that were removed from service prior to 2010						89	80

Phase 1 determined the effective useful economic life of 333 MW (summer net capacity) of the 3,228 MW (summer net capacity) of the life assessment candidates identified in Figure 2. The units designated by E.ON U.S. for evaluation in Phase 1 were: Green River 3 & 4 and Tyrone 3 coal fired steam units, and Haefling, Cane Run 11, Paddy's Run 11 & 12, and Zorn CTs. The CTs were "retired" at the end of 2009 and the coal fired steam units at the end of 2012 for the development of the Phase 1 Life Assessment Reference Plan.

Phase 2 determined the effective useful economic life of the remainder of the 3,228 MW of the life assessment candidates, or 2,895 MW. The effective useful economic lives determined in Phase 1 were incorporated into a newly developed Phase 2 Life Assessment Reference Plan as well as the plans that incorporate each Phase 2 life assessment candidate. All the candidate units included in Phase 2 were either coal fired steam or hydro units, so all of these units were assumed to "retire" at the end of 2012 for the purposes of developing the Phase 2 Life Assessment Reference Plan.

NewEnergy employed a *differential annual revenue requirements* methodology to determine the appropriate effective useful economic life for each unit. The first step involves assuming all the candidate units are "retired" in a specific year. For the life assessment candidates; combustion turbines (CTs) were "retired" at the end of 2009 and the coal and hydro units were "retired" at the end of 2012. These dates were chosen to correspond to the dates when equivalent replacement capacity could be installed. Then, a Reference Plan of replacement capacity was selected by Strategist's PROVIEW resource optimization module. This Reference Plan contains an appropriate mix of peaking, mid-range, and baseload capacity to meet future demand and energy requirements in a least cost method. These capacity types are represented by simple cycle combustion turbines, combined cycle combustion turbines, and coal fired steam generation, respectively.

The alternative resources available for developing the Life Assessment Reference Plans are described briefly in Figure 3. In addition to the annual maximum additions shown for each alternative, these resources were further restricted so that only one large coal unit, of any type, could be added in any one year. This restriction was adopted to limit capital outlay exposure. The only exception to this restriction was for 2013 during the Phase 2 Reference Plan optimization where a large portion of E.ON U.S.'s coal generating assets was "retired" and required more than one coal unit to replace that capacity. In that case, such a limitation would have left the system well below the required minimum reserve margin (see section F; "Results – Phase 2"). Combined Cycle and Simple Cycle Combustion Turbine generators were not limited against the other alternatives. The target minimum reserve margin constraint for the model optimization runs to develop the Life Assessment Reference Plans was set to 2% before 2010, and to 13.71%, 11.75%, and 10.63% for the years 2010, 2011, and 2012 respectively. The minimum target for 2010 through 2012 was adopted to maintain at least the same reserve margin of the base system with no retirements. The low reserve margin target before 2010 reflects an inability to build any new capacity prior to that time. After 2012, the target minimum reserve margin constraint was set to 14%. The 14% reserve margin minimum target from 2013 on reflects the desired long term minimum reserve margin for the system.

Figure 3:

Replacement Capacity Alternatives

Alternative Name	Description	Operating Life	Capacity	Capital Cost	First Year Available	Max per year	Study Period Max
LUSC	Ultra-Super Critical PC	50 years	766 MW	$1,906,270,000	2013	1	10
US_C	Ultra-Super Critical PC with Carbon Sequestration	50 years	613 MW	$2,756,233,000	2013	1	10
IGCC	Integrated Gasification Combined Cycle	50 years	611 MW	$1,758,982,000	2013	1	10
IG_C	Integrated Gasification Combined Cycle with Carbon Sequestration	50 years	488 MW	$2,146,299,000	2013	1	10
LGSC	Super Critical PC	50 years	766 MW	$1,862,896,000	2013	1	10
LG_C	Super Critical PC with Carbon Sequestration	50 years	613 MW	$2,718,858,000	2013	1	10
CCCT	Combined Cycle Combustion Turbine	40 years	552 MW	$465,368,900	2011	1	10
SCCT	Simple Cycle Combustion Turbine	30 years	181 MW	$78,687,500	2010	4	25

Capital Cost Values are shown in 2006$

Once the Reference Plan was developed, the replacement capacity was converted to "deferral capacity". The replacement resources designated as "deferrable" have their capacity adjusted to maintain the same reserve margin as the Reference Plan for all plans with Life Assessment candidate units included. Fixed O&M and capacity costs were also adjusted accordingly. In any year, the last unit added in the Reference Plan is the first one from which capacity is deferred. Due to the relatively high capital costs of the Carbon Sequestration units added in the later years, the Life Assessment candidate units were always less expensive to retain than the replacement carbon sequestration units. Since there were several years of negative PV annual revenue requirements differentials preceding the first of the carbon units, carbon sequestration units were not included in the deferrable capacity.

The basic system modeling was supplemented with specific cost data for each of the candidate units; projecting their O&M costs, capital expenditures (CapEx), property tax and insurance costs, as well as depreciation expenses out to 2035. These are discussed in more detail below. It is widely recognized that operating parameters such as EFOR, maintenance outage requirements, and heat rates increase (degrade) over the lifetime of an asset. Projections of future performance for aging generators would, ideally, be based on such data. However, no reliable source of data to project this performance degradation over the life of an asset currently exists. Thus, NewEnergy instead adopted the assumption that maintenance and capital expenditures would increase over the lifetime of the asset to hold performance at average lifetime levels. Data from OEM sources to support and model this assumption both exists and is readily available.

Fixed O&M costs and total capital costs (represented by the resource's Economic Carrying Charge) of the deferrable resources are also adjusted to reflect their computed capacities. The model is then run to determine the production costs for this adjusted system

The next step develops plans where each of the candidate units is not retired and assumes that each unit will then remain in service for at least 30 years. The Present Value (PV) of the

annual revenue requirements is extracted from the model for each plan retaining one of the candidate units. The difference between these PV annual revenue requirements and the PV annual revenue requirements of the Reference Plan is then computed. The first year the difference is negative (the retention costs more than the retirement) is determined and this indicates the earliest potential date for the end of the asset's effective useful economic life. The PV annual revenue requirements differentials are then accumulated from that year forward and the point where the sum turns negative and remains negative is the latest potential date for the end of the asset's effective useful economic life. This is shown in the example in Figure 4; the earliest year that the example unit would reach the end of its effective useful economic life in this case is 2014, with the latest economic retirement in 2018.

A possible situation, which does arise with some Phase 2 units, is that the first negative year for PV annual revenue requirements occurs relatively early, and then several years with positive PV annual revenue requirements follow before the annual PV differential values become negative again. This results in pushing the end of the asset's effective useful economic life out by several years while an accumulated positive differential sum is eliminated by the subsequent accumulation of negative differentials. It is not reasonable to wait until all the benefits accumulated during the intervening positive differential years are eliminated by retaining the unit for several years of negatives. In these cases, it is sensible to ignore the first occurrence of a negative differential, and to wait for the differential series to show stable negatives before beginning the summation.

It is possible for the methodology to indicate *no* end of effective useful economic life for a particular unit in the time frame of the study; in this case through 2035. This means that, based upon the assumptions used, the actual end of the asset's effective useful economic life is beyond 2035.

Figure 4:

Illustration of the Determination of the Effective Useful Economic Life For a Life Assessment Candidate Unit

Year	Differential Annual Revenue Requirements	Cumulative NPV of Differential Annual Revenue Requirements (2014 and beyond)
2010	$1.00	
2011	$1.50	
2012	$0.80	
2013	$0.60	
2014	($0.03)	($0.03)
2015	($0.50)	($0.53)
2016	$0.40	($0.13)
2017	$0.30	$0.17
2018	($0.50)	($0.33)
2019	($0.70)	($1.03)
2020	($1.00)	($2.03)
2021	($0.60)	($2.63)
2022	($0.20)	($2.83)
2023	$0.20	($2.63)
2024	$0.50	($2.13)
2025	($0.80)	($2.93)
2026	($0.10)	($3.03)
2027	$0.05	($2.98)
2028	$0.01	($2.97)
2029	($0.40)	($3.37)
2030	($0.10)	($3.47)
2031	($0.50)	($3.97)
2032	$0.30	($3.67)
2033	$0.50	($3.17)
2034	($0.30)	($3.47)
2035	($0.10)	($3.57)

C. Model Data and Assumptions:

E.ON U.S. provided NewEnergy with their latest Strategist database, translated from a PowerBase database. This basic data included all operating parameters and costs for the existing generation units in the KU and LG&E system. This includes EFOR, scheduled outage requirements, heat rates, variable and fixed operating and maintenance costs for all the generating assets, as well as load and fuel cost forecasts over the study horizon (2006 to 2035). A loads and resources summary report from the Strategist model reflecting only the existing system for selected years over the study horizon is shown in Figure 5.

Figure 5:

Loads and Resources 2006 - 2035

	2006	2010	2015	2020	2025	2030	2035
LOADS							
=====							
PEAK BEFORE DSM	6948.3	7434	8023	8597	9142	9735	10313
+ DSM ADJUSTMENTS	-112.3	-162.5	-167.4	-165.4	-141.9	-138.7	-138.7
FINAL PEAK	6836	7271.5	7855.6	8431.6	9000.1	9596.3	10174.3
RESOURCES							
=========							
TOTAL HYDRO	59.6	75.5	94.9	94.9	94.9	94.9	94.9
TOTAL THERMAL	7724.9	8099.2	8099.2	8099.2	8099.2	8099.2	8099.2
TOTAL CAPACITY	7784.5	8174.7	8194.1	8194.1	8194.1	8194.1	8194.1
RESERVES							
========							
RESERVE (MW)	948.6	903.2	338.5	-237.5	-806	-1402.2	-1980.2
RESERVE MARGIN PERCENT	13.88	12.42	4.31	-2.82	-8.96	-14.61	-19.46
CAPACITY MARGIN PERCENT	12.19	11.05	4.13	-2.9	-9.84	-17.11	-24.17

Historical O&M costs and capital expenditure streams for individual units are significantly volatile with large expenditures in some years and very little expenditures in others. This creates problems in projecting the forward trajectory for these costs. Furthermore, Capital Expenditures should be amortized over the remaining life of the asset. Some of these Capital Expenditure (CapEx) outlays would also be expected to extend the life of the asset, requiring a rolling realignment of capital depreciation for every year of the asset's remaining life. Strategist is, unfortunately, unable to handle this internally so a complex spreadsheet calculation would be required to determine the proper annual revenue requirements impacts associated with CapEx. This procedure is both unwieldy and error prone; so a simplifying assumption to treat the CapEx outlays as if they were expenses for the "extended" life of the retained assets was made.

Projections of the depreciation streams were also needed. It was assumed that since the candidate resources all are retired at specific times (the end of 2009 for CTs, the end of 2012 for Hydro and Coal Steam units), that any net plant balance at that time would have to be reallocated over the assumed additional 30 year life of the resource if it is retained. The depreciation was calculated using straight line depreciation. The calculation of property tax and insurance costs were determined by E.ON U.S. experts in those areas.

All five of these cost streams (O&M, capital expenditures, depreciation, property taxes, and insurance) were then added together for each year of the "extended life" of the asset and overlaid on the Fixed O&M Cost within the Strategist model's database for each candidate unit.

Finally, the candidate units were overlaid on the Reference Plan one at a time and the Present

Value of each year's revenue requirements (equivalent to the PV Utility Cost model output from PROVIEW) was extracted from the model and the differentials with the Reference Plan calculated.

D. Results – Reference Plan

The Life Assessment Reference Plans developed for Phase 1 and Phase 2 are shown below in Figure 6. Please note that the large number of units added in 2013 for the Phase 2 Reference Plan is the result of "replacing" the large amount of capacity that the candidate units represent. For Phase 2, two units were again needed in 2018 due to capacity that had reached the end of its effective useful economic life as projected from Phase 1. These "retirements" were included in the underlying base data for Phase 2.

Figure 6:

Life Assessment Reference Plans

	Phase 1 Reference Plan	Phase 2 Reference Plan
2006		
2007		
2008		
2009		
2010	SCCT(1)	
2011		SCCT(1)
2012		
2013	LGSC(1)	LGSC(7)
2014	SCCT(1)	
2015	SCCT(1)	SCCT(1)
2016	SCCT(1)	SCCT(1)
2017		SCCT(1)
2018	LG_C(1)	SCCT(2)
2019		SCCT(1)
2020		SCCT(1)
2021		SCCT(1)
2022	LG_C(1)	LG_C(1)
2023		
2024		
2025		
2026	IG_C(1)	IG_C(1)
2027		
2028		
2029	LGSC(1)	
2030		SCCT(1)
2031		IG_C(1)
2032		
2033		
2034		SCCT(1)
2035	LG_C(1)	SCCT(1)
2036		IG_C(1)
P.V. UTILITY COST:		
PLANNING PERIOD	$ 18,235,858	$ 23,785,290
END EFFECTS PERIOD	$ 9,224,502	$ 10,936,946
STUDY PERIOD	$ 27,460,360	$ 34,722,236

E. Results – Phase 1:

The numeric results of Phase 1 are presented in Figures 7 and 8. The end of effective useful economic lives for the coal fired steam generation in Phase 1, Green River 3 & 4 and Tyrone 3, are all 2018. Note that the first year with a negative value for Green River 3 is 2016, but the positive value in 2017 offsets this, as well as the negatives in the next several years, delaying the next accumulated negative until 2021. For this reason the negative value in 2016 is ignored, resulting in a projected end of effective useful economic life for Green River 3 in 2018. None of the peaking turbines show a projected end of effective useful economic life. This is due to the fact that once sufficient new peaking capacity is added, these units generate at very low capacity factors and the overall cost of retaining this capacity is relatively low.

Figure 7:

Phase 1

Present Value Utility Cost Differentials vs. All New Build Plan

(PVUC New Build - PVUC Existing Unit)

	Coal Steam Green River 3	Coal Steam Green River 4	Coal Steam Tyrone 3	Gas CT Cane Run 11	Gas CT Haefling	Gas CT Paddy's Run 11	Gas CT Paddy's Run 12	Gas CT Zorn	All New Build
2006	$0	$0	$0	$0	$0	$0	$0	$0	$0
2007	$0	$0	$0	$0	$0	$0	$0	$0	$0
2008	$0	$0	$0	$0	$0	$0	$0	$0	$0
2009	$0	$0	$0	$0	$0	$0	$0	$0	$0
2010	$0	$0	$0	$270	$2	$290	($146)	$430	$0
2011	$0	$0	$0	$618	$1,607	$517	$1,080	$628	$0
2012	$0	$0	$0	$611	$1,542	$518	$1,042	$622	$0
2013	$2,556	$3,583	$2,728	$980	$2,472	$838	$1,615	$992	$0
2014	$711	$1,089	$782	$542	$1,367	$463	$925	$555	$0
2015	$738	$961	$853	$480	$1,275	$434	$841	$525	$0
2016	($159)	$802	$619	$480	$1,234	$414	$824	$494	$0
2017	$624	$930	$132	$454	$1,137	$391	$780	$468	$0
2018	($2)	($38)	($49)	$436	$1,078	$379	$741	$451	$0
2019	($60)	($604)	($68)	$392	$980	$339	$662	$406	$0
2020	($322)	($162)	($169)	$347	$934	$322	$619	$386	$0
2021	($265)	($181)	($140)	$344	$869	$300	$602	$359	$0
2022	($460)	($548)	($452)	$325	$819	$283	$565	$339	$0
2023	($589)	($561)	($604)	$305	$779	$266	$531	$319	$0
2024	($485)	($701)	($949)	$281	$726	$244	$495	$295	$0
2025	($511)	($725)	($651)	$244	$652	$229	$446	$276	$0
2026	($491)	($1,081)	($635)	$249	$625	$218	$437	$262	$0
2027	($507)	($764)	($648)	$227	$572	$200	$401	$240	$0
2028	($549)	($827)	($667)	$228	$545	$204	$385	$240	$0
2029	$744	$983	$658	$453	$1,159	$393	$773	$466	$0
2030	$426	$908	$606	$405	$1,083	$363	$707	$431	$0
2031	$535	$689	$221	$383	$971	$333	$652	$394	$0
2032	$459	$590	$377	$346	$891	$301	$597	$357	$0
2033	$262	$85	$174	$300	$755	$262	$513	$310	$0
2034	$237	$287	$151	$277	$706	$242	$478	$287	$0
2035	$616	$813	$550	$336	$881	$302	$579	$357	$0

Figure 8:

Phase 1

Accumulated PV Utility Cost from First Year with a Negative Differential

	Coal Steam Green River 3	Coal Steam Green River 4	Coal Steam Tyrone 3	Gas CT Cane Run 11	Gas CT Haefling	Gas CT Paddy's Run 11	Gas CT Paddy's Run 12	Gas CT Zorn	All New Build
2006									$0
2007									$0
2008									$0
2009									$0
2010							($148)		$0
2011							$933		$0
2012							$1,975		$0
2013							$3,590		$0
2014							$4,515		$0
2015							$5,357		$0
2016							$6,181		$0
2017							$6,961		$0
2018	($2)	($38)	($49)				$7,702		$0
2019	($62)	($542)	($117)				$8,364		$0
2020	($386)	($704)	($286)				$8,983		$0
2021	($650)	($886)	($436)				$9,584		$0
2022	($1,110)	($1,433)	($879)				$10,149		$0
2023	($1,899)	($1,894)	($1,483)				$10,680		$0
2024	($2,463)	($2,695)	($2,431)				$11,175		$0
2025	($2,994)	($3,420)	($3,083)				$11,622		$0
2026	($3,486)	($4,600)	($3,717)				$12,058		$0
2027	($3,992)	($5,267)	($4,366)				$12,460		$0
2028	($4,541)	($6,094)	($5,033)				$12,845		$0
2029	($3,797)	($5,111)	($4,375)				$13,618		$0
2030	($3,271)	($4,203)	($3,769)				$14,325		$0
2031	($2,836)	($3,614)	($3,548)				$14,978		$0
2032	($2,378)	($2,924)	($3,172)				$15,574		$0
2033	($2,116)	($2,839)	($2,998)				$16,087		$0
2034	($1,879)	($2,552)	($2,847)				$16,565		$0
2035	($1,263)	($1,739)	($2,297)				$17,144		$0

F. Results – Phase 2:

Phase 2, utilized the demonstrated methodology from Phase 1. In developing the Reference Plan for Phase 2, a significant capacity shortfall occurs in 2013, primarily due to the large amount of candidate unit capacity "retiring" for the Reference Plan but also due to demand growth. Multiple coal fired technology units were required to overcome this shortfall. The numbers of each alternative unit required to cover the shortfall is shown in Figure 9.

Figure 9:

Capacity Additions to Cover 2013 Shortfall

Capacity Needed	
5190 MW	Includes Ghent 3 & 4, and Mill Creek 3 & 4
2895 MW	Excludes Ghent 3 & 4, and Mill Creek 3 & 4

	Max Capacity	Deration %	Summer Rating	Number to meet 5290 MW need	Number to meet 2895 MW need
LUSC	766	3.66%	737.9644	7.033	3.923
LGSC	766	3.50%	739.19	7.021	3.916
IGCC	611	10.97%	543.9733	9.541	5.322
LG_C	612.8	3.50%	591.352	8.777	4.896
CCCT	552	13.88%	475.3824	10.918	6.090
SCCT	181	18.23%	148.0037	35.068	19.560
IG_C	488.8	10.97%	435.17864	11.927	6.652
US_C	612.8	3.66%	590.37152	8.791	4.904

Note: Ghent 3 & 4, and Mill Creek 3 & 4 were initially considered as candidate units when the Phase 2 Reference Plan was developed. The Reference Plan shown for Phase 2 in Figure 2 was developed using the 5190 MW need in 2013. A Reference Plan using the 2895 MW need would have only required 4 LUSC units in 2013 to cover the reserve shortfall from "retiring" the Phase 2 candidate assets.

The final results for Phase 2 are presented in Figures 10 and 11. Most of the projected end of effective useful economic life schedules for this group of units fall in the 2026 to 2028 time frame: Ghent 1 in 2026, Ghent 2 in 2027, Mill Creek 1 and 2 in 2026, and all three Brown units in 2026. Brown 2 shows an early negative in 2015, but this should be ignored. Cane Run 4 retires in 2018, Cane Run 5 retires in 2022, and Cane Run 6 retires in 2023. Both of the hydro plants, Dix Dam and Ohio Falls, show an effective useful economic life throughout the study period.

Figure 10:
Phase 2
Present Value Utility Cost Differentials vs. All New Build Plan
(PVUC New Build - PVUC Existing Unit)

	Brown 1	Brown 2	Brown 3	Cane Run 4	Cane Run 5	Cane Run 6	Dix Dam	Ghent 1	Ghent 2	Mill Creek 1	Mill Creek 2	Ohio Falls	All New Build
2006	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
2007	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
2008	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
2009	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
2010	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
2011	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
2012	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
2013	$6,166	$10,801	$33,006	$6,925	$9,499	$13,584	$3,066	$36,183	$40,630	$18,860	$19,578	$10,853	$0
2014	$4,981	$6,603	$30,791	$6,200	$8,619	$12,549	$2,971	$32,362	$37,562	$9,539	$18,224	$14,727	$0
2015	$2,668	($517)	$26,483	$2,979	$3,006	$9,212	$1,995	$29,656	$33,305	$13,778	$14,381	$11,769	$0
2016	$1,886	$3,517	$19,576	$66	$2,101	$1,036	$1,937	$22,755	$26,103	$7,816	$8,526	$11,618	$0
2017	$1,906	$3,527	$14,333	$65	$2,448	$3,453	$1,940	$16,888	$20,404	$5,457	$4,111	$11,611	$0
2018	$2,097	$3,893	$12,675	($1,838)	$2,878	$3,914	$1,942	$13,697	$17,454	$4,569	$6,633	$11,670	$0
2019	$2,063	$3,939	$11,906	$325	$2,800	$4,072	$1,910	$13,625	$16,298	$6,290	$6,559	$11,710	$0
2020	$2,036	$3,370	$12,128	$157	$2,585	$3,808	$1,910	$12,596	$15,884	$5,500	$6,097	$11,706	$0
2021	$1,478	$3,407	$12,156	$216	$2,696	$3,850	$1,921	$11,708	$15,528	$6,182	$6,085	$11,725	$0
2022	$840	$742	$5,231	($1,704)	($1,550)	$992	$1,753	$4,953	$8,190	$2,180	$2,425	$10,709	$0
2023	$735	$1,244	$4,634	($1,837)	$337	($1,187)	$1,786	$4,249	$7,412	$1,992	$2,130	$10,836	$0
2024	$518	$892	$3,623	($2,062)	$116	$187	$1,820	$3,195	$5,972	$1,392	$1,575	$10,892	$0
2025	$443	$804	$2,936	($3,979)	$14	$61	$1,801	$2,465	$5,416	$1,292	$72	$11,016	$0
2026	($202)	($32)	($1,187)	($2,709)	($750)	($1,067)	$1,682	($2,155)	$1,069	($1,226)	($166)	$10,469	$0
2027	($353)	($327)	($1,754)	($2,951)	($1,035)	($1,474)	$1,687	($3,070)	($73)	($740)	($599)	$10,574	$0
2028	($972)	($921)	($3,226)	($3,486)	($1,587)	($2,149)	$1,675	($4,410)	($1,680)	($1,489)	($1,446)	$10,698	$0
2029	($688)	($1,481)	($3,940)	($3,510)	($3,154)	($2,423)	$1,686	($5,255)	($2,529)	($1,850)	($1,746)	$10,674	$0
2030	($666)	($1,133)	($4,210)	($3,534)	($1,842)	($3,874)	$1,651	($5,706)	($3,007)	($1,988)	($1,939)	$10,457	$0
2031	($515)	($1,101)	($5,476)	($3,414)	($1,752)	($2,438)	$1,508	($6,844)	($4,038)	($1,955)	($1,795)	$9,508	$0
2032	($606)	($1,056)	($5,126)	($4,621)	($1,676)	($2,360)	$1,433	($6,321)	($3,695)	($1,845)	($1,801)	$9,090	$0
2033	($602)	($1,002)	($4,026)	($3,225)	($1,636)	($2,266)	$1,375	($5,346)	($2,598)	($1,690)	($2,300)	$8,723	$0
2034	($570)	($950)	($3,684)	($3,121)	($1,572)	($2,229)	$1,313	($4,729)	($2,568)	($2,115)	($1,593)	$8,316	$0
2035	($771)	($841)	($2,904)	($2,964)	($1,469)	($2,147)	$1,260	($3,645)	($1,940)	($1,347)	($1,449)	$7,968	$0

Figure 11:
Phase 2
Accumulated PV Utility Cost from First Year with a Negative Differential

	Brown 1	Brown 2	Brown 3	Cane Run 4	Cane Run 5	Cane Run 6	Dix Dam	Ghent 1	Ghent 2	Mill Creek 1	Mill Creek 2	Ohio Falls	All New Build
2006													
2007													
2008													
2009													
2010													
2011													
2012													
2013													
2014													
2015													
2016													
2017													
2018				($1,838)									
2019				($1,513)									
2020				($1,356)									
2021				($1,140)									
2022				($2,843)	($1,560)								
2023				($4,680)	($1,223)	($1,187)							
2024				($6,743)	($1,107)	($1,000)							
2025				($10,722)	($1,093)	($939)							
2026	($202)	($32)	($1,187)	($13,431)	($1,843)	($2,006)		($2,155)		($1,226)	($166)		
2027	($554)	($359)	($2,941)	($16,362)	($2,878)	($3,480)		($5,224)	($73)	($1,966)	($765)		
2028	($1,527)	($1,280)	($6,167)	($19,877)	($4,485)	($5,529)		($9,635)	($1,753)	($3,435)	($2,211)		
2029	($2,215)	($2,760)	($10,106)	($23,386)	($7,618)	($8,052)		($14,890)	($4,282)	($5,285)	($3,956)		
2030	($2,900)	($3,894)	($14,316)	($26,921)	($9,460)	($11,935)		($20,596)	($7,289)	($7,273)	($5,897)		
2031	($3,516)	($4,994)	($19,792)	($30,335)	($11,211)	($14,364)		($27,440)	($11,327)	($9,238)	($7,693)		
2032	($4,121)	($6,050)	($24,918)	($34,956)	($12,888)	($16,724)		($33,761)	($15,022)	($11,073)	($9,492)		
2033	($4,723)	($7,053)	($28,944)	($38,181)	($14,523)	($18,989)		($39,107)	($17,620)	($12,763)	($11,292)		
2034	($5,293)	($8,002)	($32,627)	($41,302)	($16,096)	($21,219)		($43,835)	($20,188)	($14,878)	($13,385)		
2035	($6,064)	($8,844)	($35,531)	($44,266)	($17,565)	($23,365)		($47,481)	($22,129)	($16,225)	($14,833)		

G. Summary

NewEnergy Associates, LLC performed a Life Assessment of E.ON U.S.'s generating assets to determine the effective useful economic lives of these assets. Figure 12 summarizes the results of this Life Assessment study and shows the projected end of useful economic life for E.ON U.S.'s coal fired steam assets. The assessment of the economics of continuing to operate E.ON U.S.'s combustion turbine assets; the Haefling units, Cane Run 11, Paddy's Run 11 & 12 and Zorn 1, indicates that these assets should continue to be economic throughout the time horizon of the study (through 2035).

Figure 12:

End of Economic Life

Unit Name	Projected End of Economic Life
Brown 1	2026
Brown 2	2026
Brown 3	2026
Cane Run 4	2018
Cane Run 5	2022
Cane Run 6	2023
Ghent 1	2026
Ghent 2	2027
Green River 3	2018
Green River 4	2018
Mill Creek 1	2026
Mill Creek 2	2026
Tyrone 3	2018

H. Appendices

Appendix A
Project Tasks by Phase

Task No. / Phase No.	Task Description	Lead	Support	Comments
Task1, Phase 1	Develop a Strategist expansion plan with 600 MW of life assessment candidate units (out of a potential of 2,995 MW of life assessment candidate units) "retired in 2010 (CTs) and 2012 (coal). This plan will be the Phase 1 Life Assessment Reference Plan. For the purposes of this study the E.ON system will be modeled as an isolated system (i.e. - market sales and purchases will not be modeled).	NewEnergy	E.ON	NewEnergy will rely on E.ON data for this analysis, including all existing and new unit parameters, fuel costs, emission allowance costs, etc. The cost of retiring units along with any unrecovered book costs will be incorporated into the revenue requirements of the Phase 1 Life Assessment Reference Plan. New Energy will work with E.ON to develop these costs in Task 2.
Task 2, Phase 1	For each retirement candidate unit (or combination of units) develop cost data for (a) retiring the unit and (b) maintaining the unit in operation. For units that remain in operation develop forecasted operating parameters (EFOR, Scheduled outage requirements) if this will change as the unit continues operation.	E.ON	NewEnergy	NewEnergy will assist E.ON in developing the cost framework and will review the results to ensure completeness. Forecasted operating parameters will be E.ON's responsibility
Task 3, Phase 1	Employing the "deferral capacity" logic in Strategist to keep installed reserves constant, add each retirement unit (or combination of units) back into the system and recalculate the expansion plan's costs. Using the economic carrying charge to model the impacts of deferring investment costs, construct an economic ranking of all retirement candidates (or combination), showing the NPV of each candidate's impact vs. the Life Assessment Reference Plan and the Year-by-year cumulative NPV. Identify each life assessment candidate's retirement date using the approach described in this proposal.	NewEnergy	E.ON	The deferral capacity logic in Strategist will permit the retirement candidate to be evaluated by keeping reserves or reliability (or a combination thereof) constant. It defers a rolling "slice" of new capacity, thereby incorporating the net capital and operating revenue requirements and dispatch impacts of the adjusted new capacity and the retirement candidate into the analysis.
Task 4, Phase 1	Develop a draft PowerPoint presentation of results for E.ON review and incorporate E.ON comments to finalize it. Present the results at E.ON's offices in Louisville. Prepare and transfer Strategist data files and other data used for the study to E.ON.	NewEnergy	E.ON	
Task1, Phase 2	Develop a Strategist expansion plan for the remainder of the 2,995 MW of life assessment candidate units **not evaluated in Phase 1.** Incorporate any Phase 1 retirements into Phase 2 and develop a Phase 2 Life Assessment Reference Plan. For purposes of this study, the E.ON system will be modeled as it was modeled in Phase 1 (i.e.: as an isolated system, without any market sales and purchases).	NewEnergy	E.ON	NewEnergy will rely on E.ON data for this analysis, including all existing and new unit parameters, fuel costs, emission allowance costs, etc. The cost of retiring units along with any unrecovered book costs will be incorporated into the revenue requirements of the Phase 1 Life Assessment Reference Plan. New Energy will work with E.ON to develop these costs in Task 2.
Task 2, Phase 2	For each retirement candidate unit (or combination of units) develop cost data for (a) retiring the unit and (b) maintaining the unit in operation. For units that remain in operation develop forecasted operating parameters (EFOR, Scheduled outage requirements) if this will change as the unit continues operation.	E.ON	NewEnergy	NewEnergy will assist E.ON in developing the cost framework and will review the results to ensure completeness. Forecasted operating parameters will be E.ON's responsibility
Task 3, Phase 2	Same as Task 3, Phase 1	NewEnergy	E.ON	Same as Task 3, Phase 1
Task 4, Phase 2	Same as Task 4, Phase 1 with the addition of a written report covering all assumptions, modeling and results from both Phase 1 and Phase 2.	NewEnergy	E.ON	

Attachment to Response to
LGE KIUC-2 Question No. 80

Attachment No. 4

Report

NO. EA07E114

Annual Report on Form 20-F

Disclosure Controls and Procedures (DC&P) Testing

at

E.ON U.S. LLC (EUS)

February 27, 2007

Distribution List:

E.ON AG
Dr. Holtmann (Audit)
Mr. Kolpatzik

E.ON US
Mr. Rives
Ms. Scott

TABLE OF CONTENTS

1. Preamble

1.1. Job Assignment

The testing of the Disclosure Controls and Procedures over the Form 20-F is part of the regular, group wide testing of the effectiveness of the defined disclosure controls and procedures. The testing is co-coordinated by E.ON AG Audit. It was conducted within the scope of the E.ON U.S. LLC (EUS) audit plan approved by the EUS Audit Committee for 2007.

1.2. Performance

Auditor:	Fernando Rubio, Financial and Contract Auditor
Site:	E.ON U.S. LLC
Duration:	February 20, 2007 – February 23, 2007

1.3. Scope

The scope of this review included the descriptive text and statistical data for the EUS section of the Form 20-F and the Annual Report for the year ended December 31, 2006. The review included an examination of the preparation process and changes to the process from the previous year.

1.4. Testing Procedures

Audit Services compared the EUS section of the Form 20-F with the Disclosure Controls and Procedures Form 20-F spreadsheet to ensure that all applicable EUS sections were appropriately assigned. Additionally, Audit Services reviewed the entire EUS section of the Form 20-F for 2006. All subsections which contained dollar amounts, percentages, or other numerical support were

tested. These subsections were verified, when applicable, to the previous year Form 20-F, the 2006 10K draft for Louisville Gas and Electric Company (LG&E), the 2006 Annual Report for Kentucky Utilities Company (KU), or to the proper documentation and supporting records maintained by Corporate Accounting. The risk associated with each subsection is low to moderate as these items are captured in the Form 20-F footnote section. The following items contained information that was independently verified by Audit Services:

Item 3: Operational

- Environmental Liability

Item 4: Business Overview

- Core Energy Business
- U.S. Midwest
    - Overview
    - Operations
    - Market Environment
    - Regulated Business
    - Power Generation
    - Transmission
    - Distribution/Retail
    - Non-regulated Business
    - Other
- Discontinued Operations
- Regulatory Environment
    - Retail Electric Rate Regulation
    - Transmission Developments
- Environmental Matters
    - U.S. Midwest
- Property Plant and Equipment
    - Production Facilities

Item 5: Results of Operations

- Sales of U.S Midwest Market Unit (2006)
- Adjusted EBIT of U.S. Midwest Market Unit (2006)

- Sales of U.S Midwest Market Unit (2005)
- Adjusted EBIT of U.S. Midwest Market Unit (2005)

Audit Services also reviewed the EUS section of the Annual Report. The information provided for the Annual Report was compared to the Form 20-F for consistency or additional independent support to ensure accuracy.

2. Executive Summary

2.1. Overall Result

EUS Disclosure Controls and Procedures over the preparation of the Form 20-F are **effective**. No control weaknesses were found.

The test results per subsection are listed in Section 3 of this report. Audit Services made a few verbal recommendations regarding the content of the Form 20-F, which ensured consistency between the 20-F and the 10K and within the U.S portion of the Form 20-F; however none of these recommendations represent an internal control gap

2.2. Action to be taken by Management

No actions are required by EUS Management.

3. The Findings in Detail

Test results of the sample subsections are listed below. No recommendations were made to the EUS Management as a result of testing.

No	Tested Subsections	Result	Recommendations
1	Core Energy Business	Effective	No Findings
2	U.S. Midwest – Overview	Effective	No Findings
3	U.S. Midwest – Operations	Effective	No Findings
4	U.S. Midwest – Market Environment	Effective	No Findings
5	U.S. Midwest – Regulated Business	Effective	No Findings
6	U.S. Midwest – Power Generation	Effective	No Findings
7	U.S. Midwest – Transmission	Effective	No Findings
8	U.S. Midwest – Distribution /Retail	Effective	No Findings
9	U.S. Midwest – Non-regulated Business	Effective	No Findings
10	U.S. Midwest – Other	Effective	No Findings
11	Discontinued Operations	Effective	No Findings
12	Regulatory Environment – Retail Electric Rate Regulation	Effective	No Findings
13	Regulatory Environment – Transmission Developments	Effective	No Findings
14	Environmental Matters – U.S. Midwest	Effective	No Findings
15	Property Plant and Equipment – Production Facilities	Effective	No Findings
16	Results of Operations – Sales of U.S. Midwest Market Unit (2006)	Effective	No Findings
17	Results of Operations – Adjusted EBIT of U.S. Midwest Market Unit (2006)	Effective	No Findings
18	Results of Operations – Sales of U.S. Midwest Market Unit (2005)	Effective	No Findings
19	Results of Operations – Adjusted EBIT of U.S. Midwest Market Unit (2005)	Effective	No Findings
20	Annual Report	Effective	No Findings

Louisville, Kentucky February 27, 2007

EUS Audit Services Department

Mrs. Shelton
Director, Audit Services

Mr. Rubio
Financial and Contract Auditor

Standard Definitions of Testing Results	The Disclosure Controls and Procedures about the tested subsections are: **Effective**; only minor control weaknesses were identified in some areas of the tested item(s). **Partly effective**; significant control deficiencies were identified in some areas. **Ineffective**; significant control deficiencies were identified, resulting (alone or in aggregate) in a material control weakness for the tested item(s).

PPL companies

Subject of Audit: IMEA/IMPA Participation Agreements

Audit Number: CA11C070

Auditors: H. L. DiEnno

Reviewers: J. E. Andriot, D. A. Shelton

Fieldwork Completed: August 11, 2011

Draft Report Issued: August 16, 2011

Final Report Issued: August 26, 2011

To:

Chief Financial Officer	S. B. Rives
Senior Vice President, Energy Services	P. W. Thompson

cc:

Chief Executive Officer	V. A. Staffieri
Treasurer	D. K. Arbough
Manager, Cash Management	R. C. Aemmer
Controller	V. L. Scott
Director, Accounting and Regulatory Reporting	S. L. Charnas
Manager, Revenue Accounting and Analysis	F. Mazza
Manager, Regulatory Accounting and Reporting	T. E. Raible
Manager, Property Accounting	S. L. Wiseman
Vice President, Energy Marketing	D. S. Sinclair
Director, Corporate Fuels and By Products	C. M. Pfeiffer
Manager, Fuels Accounting and Administration	E. N. Thompson-Long
Director, Energy Services Accounting & Budgeting	R. A. Hudson
Executive Director Corporate Audit Services (PPL)	M. F. Urban
Ernst & Young (EY)	M. Garrison
Ernst & Young (EY)	R. Furlan

LG&E and KU Energy LLC Audit Services
IMEA/IMPA Participation Agreements
CA11C070

Management Summary

Audit Services conducted an assessment of Illinois Municipal Electric Agency (IMEA) and Indiana Municipal Power Agency (IMPA) Participation Agreements for the joint ownership (25 percent) of Trimble County Units 1 and 2. The primary objectives of our audit were to

- review the Participation Agreements with IMEA and IMPA for their ownership portions of Trimble County Units 1 and 2;
- determine billings to IMEA and IMPA accurately reflect their share of operating and maintenance expenses, incremental capital assets acquired, and fuel used; and
- determine if energy transactions are accurately accounted for and in compliance with applicable agreements.

The scope of the audit included a review of IMEA and IMPA billings between July 1, 2010 and June 30, 2011.

The audit was performed based on inquiry, observation, and document analysis. In determining sample sizes, a risk-oriented approach was applied.

A strength noted during the audit was individuals providing information for the IMEA and IMPA billings have a thorough understanding of the components for which they contribute.

Overall, management of the Participation Agreements with IMEA and IMPA is well controlled. The Participation Agreements were reviewed and billings were found to accurately reflect IMEA's and IMPA's share of operating expenses, capital assets, and fuel used as described in the Participation Agreements. This included energy transactions, which were found to be calculated and allocated between IMEA and IMPA as appropriate. No issues resulted from the audit.

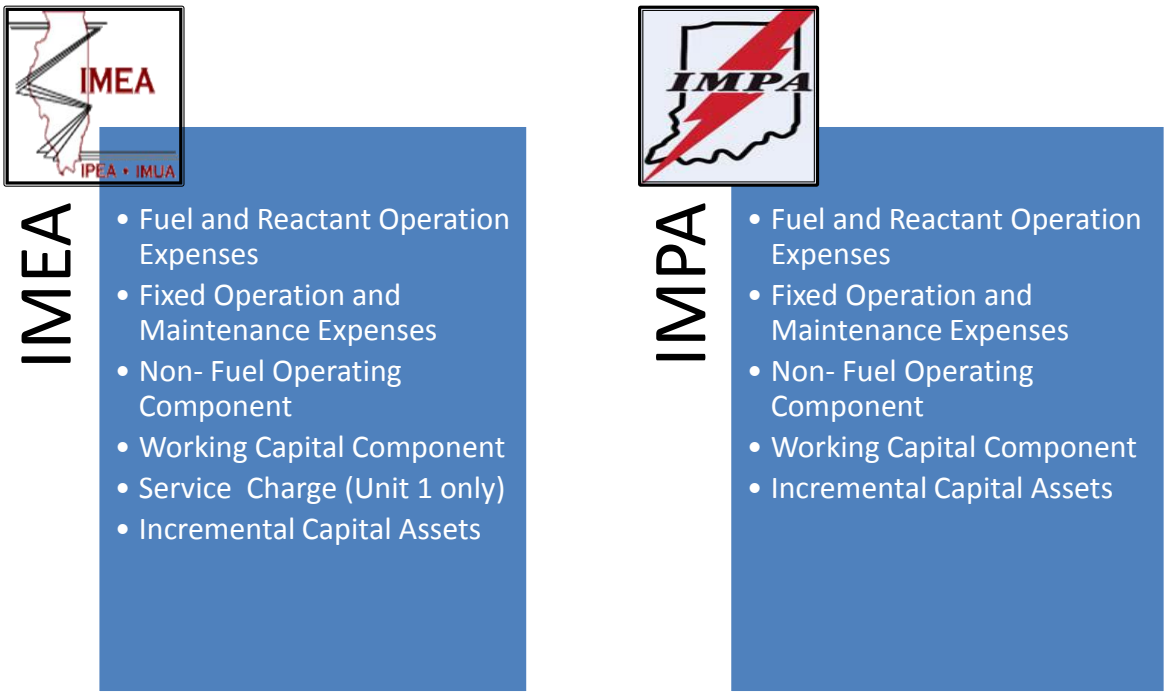
LG&E and KU Energy LLC Audit Services
IMEA/IMPA Participation Agreements
CA11C070

Background

Trimble County Unit 1 (TC1), a 495-megawatt (MW), coal-fired electric generating unit, was placed in commercial operation on December 23, 1990. The Kentucky Public Service Commission (KPSC) ordered 25 percent of the total cost of TC1 was not allowed for Louisville Gas and Electric Company (LG&E) rate-making purposes. In September 1990, LG&E agreed to sell a 12.12 percent ownership interest in TC1 to IMEA. In February 1993, the remainder of the disallowed portion (12.88 percent) was sold to IMPA.

The IMEA Agreement and the IMPA Agreement provide each agency with rights of first refusal to participate in ownership of a second coal-fired generating unit at the Trimble County site. In anticipation of constructing Trimble County Unit 2 (TC2), LG&E and Kentucky Utilities Company (KU) signed the Unit 2 Participation Agreement in February 2004. It provided for joint ownership of TC2, a 760-MW unit, with IMEA and IMPA. Collectively, LG&E and KU own 75 percent of TC2, which is split 19 percent to LG&E and 81 percent to KU. IMEA and IMPA have the same ownership interests in TC2 as they do in TC1.

The Participation Agreements allow LG&E and KU to allocate to IMEA and IMPA certain costs related to TC Units 1 and 2. The major cost allocation categories are listed below.



For the twelve months ended June 30, 2011, total net billings to IMEA and IMPA, including power purchased and sold, totaled $63,080,851.

Bills are prepared by the Cash Management department monthly, based on input provided by Property Accounting, Fuels Accounting, Regulatory Accounting and Reporting, and Revenue Accounting.

Auditing Procedures Performed

Review of IMEA and IMPA Billings

Four months of IMEA/IMPA billings were randomly selected for review. These billings included amounts for both TC1 and TC2.

For October, May, and June, billings were recalculated and agreed to the supporting documentation provided by Cash Management.

April's bill was selected for in-depth review. Meetings were held with contributors to gain an understanding of their role in the billing process and to walk through the components. Amounts were recalculated based on Participation Agreement terms and agreed to the calculations prepared by the contributors. Amounts comprising the calculation were agreed to supporting documentation and source systems. Supporting documentation included journal entries, Discoverer reports, calculation spreadsheets, financial statements, Fuelworx reports, Settlement Agreements, and other documents. Source systems included Oracle Financial Management System (Oracle) and the Commodity Trading System (CTS).

For all months tested, bills were recomputed without exception and noted to be allocated between IMEA and IMPA in accordance with Agreement terms. The billings accurately reflect their share of costs for energy transactions as appropriate.

Review of Fuel Allocation

Management noted an accounting error was made in June 2010 regarding the allocation of a certain coal type. The coal inventory for Trimble County had been allocated between TC1 and TC2 based on the nameplate capacity of each unit. However, Powder River Basin (PRB) coal can only be used at TC2, and the correct allocation for this coal type is 100 percent to TC2 only. The incorrect calculation caused too much inventory to be allocated to LG&E since its TC2 ownership percentage is 19 percent compared to KU's 81 percent. The combined percentage for both TC1 and TC2 is 52 percent to LG&E and 48 percent to KU. The allocation calculation was revised for July 2010, and the error corrected.

The April, May, and June 2011 fuel allocations were recomputed, and the allocation was noted to be accurate, including proper allocation of PRB fuel.

CONFIDENTIAL

US AUDIT SERVICES

LG&E ENERGY CORP.
REPORT NO. USAS EA-03-U-122

AUDIT REPORT

LOUISVILLE GAS AND ELECTRIC COMPANY AND KENTUCKY UTILITIES COMPANY

CORPORATE FINANCE

PROPERTY ACCOUNTING CYCLE AUDIT

Date Issued: November 21, 2003

LG&E ENERGY CORP. AUDIT REPORT No. USAS EA-03-U-122

LOUISVILLE GAS AND ELECTRIC COMPANY
AND KENTUCKY UTILITIES COMPANY

CORPORATE FINANCE
PROPERTY ACCOUNTING CYCLE AUDIT

CONTENTS

Audit carried out by: N. J. Koziel, R. C. Aemmer
Report reviewed by: D. A. Shelton

Field Work Completed	September 24, 2003
Draft Report Issued	September 30, 2003
Final Report Issued	November 21, 2003

Circulation List

Full Report

S. B. Rives	Chief Financial Officer
V. A. Staffieri	Chief Executive Officer
M. Holtmann	Senior Vice President, Audit, E.ON AG
M. Söhlke	Group Chief Financial Officer
V. L. Scott	Director, Financial Planning and Accounting – Utility Operations
G. R. Skaggs	Manager, Property Accounting

Executive Summary

PwC External Auditors

Synopsis

Audit Committee

1 EXECUTIVE SUMMARY

1.1 Introduction

1.1.1 Audit Services recently completed an audit of the Property Accounting Cycle for Louisville Gas and Electric Company (LG&E) and Kentucky Utilities Company (KU). The objectives of this engagement were to identify the risks and assess the effectiveness of procedures and internal controls related to the property accounting function.

1.1.2 The scope of the audit covered the period from June 1, 2002 through May 31, 2003.

1.1.3 Audit activities included appropriate interviews; reviews and evaluation of accounting procedures and practices, and compliance with regulatory requirements; and related testwork.

1.2 Conclusion

1.2.1 Based upon the audit work performed, operational, financial and compliance controls related to the property accounting cycle for LG&E and KU were appropriate and operating effectively for the period covered by this audit.

1.3 Main Findings and Recommendations

1.3.1 General Ledger (GL) account 107001, Construction Work in Progress (CWIP), for both LG&E and KU exceeded the balances in the ORACLE Project Accounting module (the CWIP subsidiary ledger) by $20,240.99 and $67,974.90 respectively. The majority of items comprising these balancing differences had been outstanding for more than two years.

2 IMPLEMENTATION PLAN **USAS FI-03-U-122**

Implementation Meeting **Present:** Management: G. R. Skaggs, B. M. Rose
Date: September 9, 2003 Audit Services: N. J. Koziel

Recommendations	Agreed / Not Agreed	Management Action Plan	Person Responsible	Date to be Completed	Management's Follow-up Comments / Date
CWIP reconciling differences should be researched and resolved. Going forward, any reconciling differences should be resolved as part of the monthly reconciliation process.	Agreed	The CWIP reconciling differences for both LG&E and KU have been identified and appropriate adjustments have been made. No write-offs were required.	G. R. Skaggs	08/31/03	Implemented and agreed.

3 BACKGROUND

3.1.1 The Property Accounting Department, consisting of the Manager and eight Analysts, is located on the third floor of the Broadway Office Complex. As of the May 31, 2003 audit date, more than 868,000 individual assets were in the ORACLE Fixed Assets module for LG&E and KU, with a combined value of over $6.5 billion. The reserve for depreciation of these assets was over $3 billion. Additionally, the combined CWIP balance as of May 31, 2003, was approximately $620 million, consisting of 2,910 projects.

3.1.2 The Property Accounting Cycle begins with the activation of new capital projects for LG&E and KU. Approved Authorizations for Investment Proposals (AIP) are sent to the Property Accounting Department, which logs them into an Access database and activates the new project in the Project Accounting (PA) module of the ORACLE financial system.

3.1.3 Charges made to active projects are recorded to the appropriate project in PA and reflected in the CWIP General Ledger account. Property Accounting is responsible for reconciling the PA balance to CWIP on a monthly basis. Active projects remain in CWIP until they have been coded "Complete" in PA by the responsible Line of Business, and subsequently unitized (capitalized) by Property Accounting.

3.1.4 Each month, Property Accounting runs a Completion Report which returns those projects that meet the criteria of being completed for greater than 90 days. This is to ensure that all outstanding charges for a project have been paid before Property Accounting classifies it to Plant in Service.

3.1.5 To ensure timely unitization and depreciation, Property Accounting has recently initiated a quarterly report of projects that have had no activity in CWIP for more than 90 days. This report is distributed to all Budget Coordinators for follow up. The first report, as of March 31, 2003, listed 877 inactive projects; the July 31 report listed only 271. Of these, only 182 were still outstanding from the March report (approximately 20 percent of the March total). Property Accounting prioritizes higher dollar completed projects to be unitized first.

3.1.6 The process of unitizing involves transferring all costs accumulated during the construction of a project from the PA module to an active asset within the ORACLE Fixed Assets module. This is done by creating an AsBuilt, which lists the actual components of the completed projects, and is used to assign the Units of Property per Federal Energy Regulatory Commission (FERC) requirements. This also has the effect of moving the related costs from the General Ledger CWIP account to the Plant in Service account. At this point, depreciation of the asset can begin.

3.1.7 Current depreciation rates are based on a study performed by Management Resources International, Engineers and Consultants (MRI). The current rates took effect in 2001. Audit Services verified a sample of approved rates to those applied to actual fixed assets without exception.

3.1.8 Depreciation rate studies are normally performed on a five-year cycle, and rates are adjusted accordingly. Neither the FERC nor the Kentucky Public Service Commission (KPSC) has established a set period for conducting depreciation reviews. LG&E Energy Corp. (LEC) committed to the KPSC to do a new study in 2004 based on 2003 data; however, LEC has accelerated this, and instead, a study is being performed in 2003 based on 2002 data. If approved, these rates are expected to take effect as of January 1, 2004.

3.1.9 The appropriate depreciation rate is systemically applied to the cost of each depreciable asset on a monthly basis, and a depreciation reserve is established. For non-group assets, such as transportation equipment, depreciation ceases when the asset is fully depreciated. However, in the case of group assets, which comprise the majority of utility assets, depreciation continues until the asset is actually retired. Since depreciation rates are based on the unrecovered value of the group in total, rates are relatively stable over time and the correct amount of depreciation is recorded on the group as a whole. Audit testwork included recalculation of monthly and year to date depreciation expense, and the depreciation reserve, for a sample of fixed assets. No exceptions were noted.

3.1.10 If an asset is to be retired, the depreciation reserve is charged with the book value of the property retired plus the cost of removal, and credited with salvage value, if any. Property Accounting also prepares and processes entries to record any gain or loss on the sale of LG&E or KU property. Audit Services verified the propriety of accounting transactions for a sample of retired assets and one asset sold during the audit period.

3.1.11 Property Accounting is responsible for reconciling the Fixed Asset balances to the respective Plant in Service and Depreciation Reserve General Ledger accounts on a monthly basis, and for researching and resolving any differences. Audit Services tested the May 31, 2003, reconciliations of Plant in Service and Depreciation Reserve for LG&E and KU without exception.

3.1.12 Statement of Financial Accounting Standards No. 143, *Accounting for Asset Retirement Obligations* (SFAS 143), changed the way LG&E and KU measure legal asset retirement obligations (ARO) that result from the acquisition, construction, and normal operation of tangible long-lived assets. SFAS 143 provides guidance for determining when a liability should be recognized for an ARO; and if a liability is necessary, at what value that liability should be recorded. As a result of SFAS 143, Property Accounting was required to make the cumulative effect adjustments to transition all eligible existing assets to the new accounting method effective January 1, 2003. An accounting model was developed for this purpose, and appropriate journal entries to record accumulated depreciation and ARO liability from the year the asset was put into service through 2003 have been made. Audit work included review and testing of the ARO accounting model. No exceptions were noted.

3.1.13 In addition to the normal property accounting cycle, Property Accounting participates in the periodic depreciation studies performed by an external engineering and consulting company. Property Accounting also provides support regarding various regulatory matters (e.g., rate case).

4 DETAILED FINDINGS

4.1 Reconciliations of Construction Work in Progress (CWIP)

4.1.1 General Ledger account 107001, Construction Work in Progress (CWIP) for both LG&E and KU, are reconciled to the ORACLE Project Accounting module on a monthly basis. Audit Services' review of these reconciliations as of May 31, 2003, showed unidentified differences of $20,240.99 for LG&E and $67,974.90 for KU. The majority of items comprising these balancing differences had been outstanding for more than two years.

4.1.2 Failure to identify and clear reconciling differences in a timely manner could allow errors and/or misappropriations to go undetected, and thereby impact the accuracy of financial statements.

4.1.3 **Recommendation**: Property Accounting should determine if the CWIP differences for LG&E and KU warrant additional research, or if they should be written off. Going forward, reconciling differences for CWIP should be researched and cleared monthly. If an out-of-balance condition cannot be resolved in the same month, the date the difference occurred should be indicated on the reconciliation form each month until it has been cleared. All reconciliations should be printed and signed by the associate who performed the reconciliation, and reviewed and initialled by a second Property Accounting associate as evidence of this review.

ENGAGEMENT MEMO

From: Hilbert, Debbie on behalf of Balderson, Carl
Sent: Wednesday, July 02, 2003 4:12 PM
To: Rives, Brad
Cc: Staffieri, Vic; Aitken-Davies, Richard; Soehlke, Michael (PowerGen); Scott, Valerie; Skaggs, Gerald; Melanie R. Lockard (melanie.r.lockard@us.pwcglobal.com)
Subject: LG&E and KU - Property Accounting Audit Engagement Memo

Audit Services has scheduled an audit of the property accounting cycle within Louisville Gas and Electric Company and Kentucky Utilities Company, with preliminary survey work scheduled to begin the week of July 7, 2003. The objectives of this engagement are to identify the risks and assess the effectiveness of procedures and internal controls related to the property accounting function.

The scope of the audit will cover the period June 1, 2002 through May 31, 2003, and will include appropriate reviews, evaluations and testwork to determine that:

- transactions affecting property, plant, and equipment are authorized in accordance with Company policies;
- resources used, costs incurred and calculated depreciation for capital projects are promptly and accurately reported, classified, and recorded in OFMS;
- rates and estimated useful life used for depreciating capital assets are in compliance with Kentucky Public Service Commission requirements;
- gains and losses on sales of property are properly approved and accounted for;
- appropriate reconciliations of Project Accounting records to the General Ledger are performed and documented; and
- accounting procedures are in place to ensure compliance with SFAS 143, Accounting for Asset Retirement Obligations.

We will encourage the involvement of your staff in identifying process improvements during the course of our audit.

The audit will be performed by Nancy Koziel, Audit Contractor, under the direction of Bob Aemmer, Manager, Financial, Contract and Energy Marketing Auditing. We look forward to working with you and your staff during this engagement. Please advise Bob if you would like to schedule an opening conference to discuss the audit objectives, scope and timing; or you may call me with any questions or comments.

Carl

For more information on Audit Services, please visit the Audit Services Website on the Company Intranet at http://intranet1/audit/newlook .

Report

NO EA-06-E-114

Annual Report on Form 20-F

Disclosure Controls and Procedures Testing

at

E.ON U.S. LLC (EUS)

February 28, 2006

Distribution List:

E.ON AG
Dr. Holtmann (Audit)
Mr. Kolpatzik

E.ON US
Mr. Rives
Ms. Scott

TABLE OF CONTENTS

1. Preamble

1.1. Job Assignment

The testing of the Disclosure Controls and Procedures over the Form 20-F is part of the regular, group wide testing of the effectiveness of the defined disclosure controls and procedures. The testing is co-coordinated by E.ON AG Audit. It was conducted within the scope of the E.ON U.S. LLC (EUS) audit plan approved by the EUS Audit Committee for 2006.

1.2. Performance

Auditor:	Bill Zoeller, Senior Financial and Contract Auditor
Site:	E.ON U.S.
Duration:	February 22, 2006 – February 28, 2006

1.3. Scope

The scope of this review included the descriptive text and statistical data for the EUS section of the Form 20-F and the Annual Report for the year ended December 31, 2005. The review included an examination of the preparation process and changes to the process from the previous year.

1.4. Testing Procedures

Audit Services compared the EUS section of the Form 20-F with the Disclosure Controls and Procedures Form 20-F spreadsheet to ensure that all applicable EUS sections were

appropriately assigned. Additionally, Audit Services reviewed the entire EUS section of the Form 20-F for 2005. All subsections which contained dollar amounts, percentages, or other numerical support were tested. These subsections were verified, when applicable, to the previous year Form 20-F, the 2005 10K draft for Louisville Gas and Electric Company (LG&E) and Kentucky Utilities Company (KU), or to the proper documentation and supporting records maintained by the Controller. The risk associated with each subsection is low to moderate as these items are captured in the Form 20-F footnote section. The following items contained information that was independently verified by Audit Services:

Item 3: Operational

- Environmental Liability

Item 4: Business Overview

- Core Energy Business
- U.S. Midwest
    - Overview
    - Operations
    - Market Environment
    - Regulated Business
    - Power Generation
    - Transmission
    - Distribution/Retail
    - Non-regulated Business
- Discontinued Operations
- Regulatory Environment
    - Retail Electric Rate Regulation
    - Transmission Developments
- Environmental Matters
    - U.S. Midwest
- Property Plant and Equipment
    - Production Facilities

Item 5: Results of Operations

- Sales of U.S Midwest Market Unit (2005)
- Adjusted EBIT of U.S. Midwest Market Unit (2005)
- Sales of U.S Midwest Market Unit (2004)
- Adjusted EBIT of U.S. Midwest Market Unit (2004)

Audit Services also reviewed the EUS section of the Annual Report. The information provided for the Annual report was compared to the Form 20-F for consistency or additional independent support to ensure accuracy.

2. Executive Summary

2.1. Overall Result

EUS Disclosure Controls and Procedures over the preparation of the Form 20-F are **effective**. No control weaknesses were found.

The test results per subsection are listed in Section 3 of this report. Audit Services made several recommendations regarding the content of the Form 20-F, which ensured consistency between the 20-F and the 10K and within the U.S portion of the Form 20-F; however none of these recommendations represent an internal control gap.

2.2. Action to be taken by the Management

No actions are required by EUS Management.

3. The Findings in Detail

Test results of the sample subsections are listed below. No recommendations were made to the EUS Management as a result of testing.

No	Tested Subsections	Result	Recommendations
1	Core Energy Business	Effective	No Findings
2	U.S. Midwest – Overview	Effective	No Findings
3	U.S. Midwest – Operations	Effective	No Findings
4	U.S. Midwest – Market Environment	Effective	No Findings
5	U.S. Midwest – Regulated Business	Effective	No Findings
6	U.S. Midwest – Power Generation	Effective	No Findings
7	U.S. Midwest – Transmission	Effective	No Findings
8	U.S. Midwest – Distribution /Retail	Effective	No Findings
9	U.S. Midwest – Non-regulated Business	Effective	No Findings
10	Discontinued Operations	Effective	No Findings
11	Regulatory Environment – Retail Electric Rate Regulation	Effective	No Findings
12	Regulatory Environment – Transmission Developments	Effective	No Findings
13	Environmental Matters – U.S. Midwest	Effective	No Findings
14	Property Plant and Equipment – Production Facilities	Effective	No Findings
15	Results of Operations – Sales of U.S. Midwest Market Unit (2005)	Effective	No Findings
16	Results of Operations – Adjusted EBIT of U.S. Midwest Market Unit (2005)	Effective	No Findings
17	Results of Operations – Sales of U.S. Midwest Market Unit (2004)	Effective	No Findings
18	Results of Operations – Adjusted EBIT of U.S. Midwest Market Unit (2004)	Effective	No Findings
19	Annual Report	Effective	No Findings

Louisville, Kentucky February 28, 2006

EUS Audit Services Department

Mrs. Shelton
Director, Audit Services

Mr. Zoeller
Senior Financial and Contract Auditor

Standard Definitions of Testing Results	The Disclosure Controls and Procedures about the tested subsections are: **Effective**; only minor control weaknesses were identified in some areas of the tested item(s). **Partly effective**; significant control deficiencies were identified in some areas. **Ineffective**; significant control deficiencies were identified, resulting (alone or in aggregate) in a material control weakness for the tested item(s).

US AUDIT SERVICES

LG&E ENERGY

LG&E ENERGY CORP.
REPORT NO. USAS FI-02-E-255

AUDIT REPORT

LG&E ENERGY CORP.

CAPITAL INVESTMENT PROCESS

Date Issued: September 9, 2003

LG&E ENERGY CORP. AUDIT REPORT No. USAS FI-02-E-255

LG&E ENERGY CORP.
CAPITAL INVESTMENT PROCESS

CONTENTS

APPENDIX

Audit carried out by: N. J. Koziel, J. J. Logan, R. C. Aemmer
Report reviewed by: D. A. Shelton

Field Work Completed	May 14, 2003
Draft Report Issued	July 22, 2003
Final Report Issued	September 9, 2003

Circulation List

Full Report

S. B. Rives	Senior Vice President, Finance
V. A. Staffieri	Chief Executive Officer
R. Aitken-Davies	Chief Financial Officer
M. Holtmann	Senior Vice President, Audit, E.ON AG
M. Söhlke	Group Chief Financial Officer
M. G. French	Director, Financial Planning and Accounting – LGE Energy
C. Hermann	Senior Vice President, Energy Delivery
R. A. Hudson	Director, Generation Accounting and Budget
J. R. McCall	Executive Vice President, General Counsel, and Corporate Secretary
V. L. Scott	Director Financial Planning and Accounting – Utility Operations
R. Smith	Senior Vice President, Project Engineering
A. O. Tillack	Director, Planning and Controlling
P. W. Thompson	Senior Vice President, Energy Services
D. A. Vogel	Vice President, Retail and Gas Storage Operations
W. C. Welsh	Senior Vice President, Information Technology

Executive Summary

PwC External Auditors

Synopsis

Audit Committee

1 EXECUTIVE SUMMARY

1.1 Introduction

1.1.1 Audit Services has completed an audit of LG&E Energy Corp's (LEC) capital investment process. The objectives of this engagement were to:

- determine that the procedures set forth in the LEC Capital Policy are consistently followed by the business units;
- determine that project costs are being monitored while the projects are active; and
- determine that a post project analysis is conducted to ensure that cost savings and benefits are met.

1.1.2 The scope of the audit included capital projects active during the period of January 1, 2000 through October 31, 2002, and capital projects that were closed between January 1, 2002, and October 31, 2002.

1.2 Conclusion

1.2.1 The desired operational, financial and compliance controls appear to be in place, and are appropriate, documented and functioning as designed.

1.3 Main Findings and Recommendations

1.3.1 During the course of this audit, the LEC Capital Policy and the Authorization for Investment Proposal form were revised. Several of the revisions noted on these documents addressed the issues identified in this audit.

1.3.2 Investment reviews are not being performed on a consistent basis. Investment reviews are required for all capital investment projects that require Investment Committee approval.

1.3.3 Capital Investment projects often remain in an incorrect status after the project has been cancelled or after the project has been completed.

2 IMPLEMENTATION PLAN **USAS FI-02-E-255**

Implementation Meeting **Present:** Management: V. L. Scott

Date: May 14, 2003 Audit Services: J. J. Logan

Recommendations	Agreed / Not Agreed	Management Action Plan	Person Responsible	Date to be Completed	Management's Follow-up Comments / Date
4.1.3 The Investment Review requirement should be added to the revised LEC Capital Policy. The addition of this requirement will provide adequate communication and guidelines for completing an investment review. This addition to the corporate policy places the accountability for conducting the review with the Budget Coordinator.	Agreed	The Investment Review requirement will be added to the revised LEC Capital Policy.	V. L. Scott	07/31/03	Implemented
4.1.4 Guidelines for completing the Investment Review should be drafted to ensure consistency in the report's contents and formatting.	Agreed	The Planning and Controlling Group will draft guidelines for the content and formatting of the Investment Review	A. O. Tillack	11/15/03	

Recommendations	Agreed / Not Agreed	Management Action Plan	Person Responsible	Date to be Completed	Management's Follow-up Comments / Date
4.2.2 Active projects should be moved to completed status after the project is finished and no future expenditures are anticipated. The updated LEC Capital Policy sets guidelines for completing projects. These guidelines should be followed to ensure timely closure of all capital investment projects.	Agreed	The updated LEC Capital Policy will set guidelines for completing projects. These guidelines will be followed to ensure timely closure of all capital investment projects.	V. L. Scott	07/31/03	Implemented
4.3.3 The Microsoft Outlook Delegation of Authority tool should be referenced to determine if designated signatures are appropriate when signing on behalf of someone at the manager or higher level.	Agreed	Property Accounting was introduced to this tool and now it is being incorporated into their review for proper signatures.	G. R. Skaggs	04/28/03	Implemented

Recommendations	Agreed / Not Agreed	Management Action Plan	Person Responsible	Date to be Completed	Management's Follow-up Comments / Date
4.3.5 Pending projects should be monitored. Working closely with the Budget Coordinators, the head of each Business Unit has the ultimate accountability for ensuring that a Business Unit does not over commit its capital budget. If it becomes reasonably certain that a pending project will not materialize or the funds set aside for the pending project have been reallocated to an unbudgeted or over budgeted project, the project should be changed to cancelled status.	Agreed	The Authorization for Investment Proposal (AIP) form has been updated to require the Budget Coordinator's signature. This signature attests that sufficient funds are available for the capital project.	V. L. Scott	02/01/03	Implemented

3 BACKGROUND

3.1.1 The LEC Capital Policy provides the following:

- Guidelines for determining what expenditures qualify as a capital investment;
- The approval process for capital investment projects; and
- The general guidelines placed on capital investment projects.

3.2 Budgeted Capital Investment Projects

3.2.1 Annually each Business Unit identifies and budgets for the capital investment projects that it plans to start and/or complete during the calendar year. If the Business Unit anticipates that a capital project will carry over into the next calendar year, then the project's costs must be included in the next calendar year's budget. A capital budget must be approved before any project activity can commence. Before an approved project can incur any expenditures, an Authorization for Investment Proposal (AIP) must be completed and approved. The project sponsor along with the Budget Coordinator of each Business Unit is responsible for the completion of the AIP. The AIP provides information such as the project's estimated start and completion dates, project costs, reason for project, a project description and accounting information such as the responsibility center. The authority to approve an AIP follows the monetary approval guidelines defined in the LEC Engagement Authority Matrix.

3.2.2 Projects exceeding $300,000 must be reviewed by either the Financial Planning – LG&E Energy Corp. Department or the Financial Planning – Utility Operations Department. Information Technology (IT) and Development projects exceeding $500,000[1] and all other projects exceeding $1,000,000 must be approved by the Investment Committee. The Investment Committee is made up of senior level LEC officers. The committee reviews and approves high dollar capital projects to ensure that they are aligned with corporate strategic goals.

3.2.3 After the capital project has received all of the necessary approvals, the AIP is sent to Property Accounting where the project is placed in active status. An AIP for a Western Kentucky Energy (WKE) project is subject to the same approval process, except it is sent to WKE Accounting. It is at this point the project can incur charges. If during the project it becomes evident that project costs will exceed the budgeted amount by 10 percent or more a new AIP must be completed. Funding for the cost overrun must come from either cancelling or reducing other planned projects. The additional funding is subject to the same approval process as the original AIP.

3.2.4 Upon completion of the capital project, either the Budget Coordinator or project manager will notify Property Accounting of the project's status. At this point, Property Accounting will begin the necessary steps to close the capital project and unitize the asset for accounting records. If the project required the approval of the Investment Committee, the Budget Coordinator completes an Investment Review that identifies the project's actual costs and notes whether the project is providing the benefits that were stated on the AIP.

3.3 Unbudgeted Capital Investment Project

3.3.1 If the need arises for a capital investment project that was not included in the annual budget, the unbudgeted project can occur only if: (1) a project(s) with a cost equal to the unbudgeted project is cancelled; (2) there is a reduction in the scope of a budgeted project sufficient to cover the unbudgeted project; or (3) prior written approval of the CFO and CEO is

[1] As of the distribution date of this report, the threshold has been lowered to $250,000.

obtained. Approval for unbudgeted projects follows the Authority Matrix. However, all unbudgeted capital investment projects must be approved by the respective financial planning department. Unbudgeted capital expenditures are also subject to an Investment Committee review if it meets the $500,000[2] threshold for IT projects and a $1,000,000 threshold for non-IT projects.

4 DETAILED FINDINGS

4.1 Completed Capital Projects

4.1.1 Investment reviews are to be performed for completed capital investment projects that require the approval of the Investment Committee. The investment review is to be performed by the project sponsor and coordinated through the Budget Coordinator. This review takes the form of a report, provides the actual project costs, addresses whether the benefits on the AIP are being achieved, and notes any lessons learned during the project.

4.1.2 Audit Services reviewed a sample of capital expenditure projects that were completed during the audit period. For the selected projects that met the criteria for an Investment Committee approval, Audit Services followed up with the Budget Coordinator to determine that an Investment Review was completed for the project. Audit Services received mixed responses from the Budget Coordinators and expanded its inquiry to other Budget Coordinators. The second inquiry consisted of asking whether the Budget Coordinator was aware of the Investment Review requirement for Capital Projects that requires Investment Committee approval. As a result of this second inquiry, it was determined that not all coordinators were aware of the Investment Review requirement nor were they conducting the review on a consistent basis.

4.1.3 **Recommendation:** Upon the recommendation of Audit Services, the Investment Review requirement will be added to the revised LEC Capital Policy. This recommendation is the result of the April 2, 2002, memo from LG&E Energy Corp.'s Chief Financial Officer that notes an Investment Review should be completed for all capital projects that required an Investment Committee approval. The Investment Review should be prepared within two months of the project's completion. This review should be submitted to the Investment Committee and the Investment Committee reserves the right to conduct a more detailed review up to 24 months after the project's completion.

4.1.4 Also, procedures should be drafted that will provide the Budget Coordinators with guidelines for completing the investment review. These guidelines will address the content of the report along with its formatting.

4.2 Monitoring Capital Projects

4.2.1 A sample of capital expenditure projects that were either started or closed during the scope period were reviewed to ensure that project expenditures did not exceed the amount budgeted for the project. No exceptions were noted; however, Audit Services did note that projects often remain in 'active' status nine or more months after the last activity date. As a result capital expenditure projects are often in service prior to the project closure activities that are conducted by Property Accounting. When a project is closed, it is added to the Units of Property listing and unitization (depreciation) of the asset begins. An in-service project cannot be unitized or added to the Units of Property listing while it is in active status. As a result, catch up depreciation adjustments are often needed when the project is closed.

[2] As of the distribution date of this report, the threshold has been lowered to $250,000.

4.2.2 **Recommendation:** Active projects should be moved to 'completed' status after the project is finished and no future expenditures are anticipated. It is the joint responsibility of the project manager (or sponsor) and the Budget Coordinator to ensure that the necessary communication takes place. The updated LEC Capital policy sets guidelines for completing an active project. These guidelines should be followed to ensure timely closure of all capital investment projects.

4.3 Capital Expenditure Approval Process

4.3.1 Audit Services reviewed a sample of capital expenditure projects that were approved during the audit period. The support for the AIP was reviewed for completeness and to determine that all approving signatures were valid and at an appropriate level to authorize the capital expenditure project. The capital project was also traced to the budget to ensure that the project was budgeted for the current year and that the funding requested agreed with the budget.

4.3.2 During this review it was noted that Property Accounting could not always validate the approving signatures found on the AIP. This is particularly true with budgeted capital projects that are under $300,000 where someone is signing on behalf of another. Because these projects are budgeted and their amounts do not merit Investment Committee review, these projects are sent directly to Property Accounting who does not have signature cards, delegation of authority notices, memos noting personnel changes, or similar documentation to validate the approving signature.

4.3.3 **Recommendation:** The Microsoft Outlook Delegation of Authority tool should be referenced to determine if designated signatures are appropriate when signing on behalf of someone at the manager or higher level. Property Accounting was introduced to this tool during the review and is now referencing the tool to ensure that proper signatures are obtained.

4.3.4 Audit Services also noted that pending projects were not always changed to 'cancel' status once the funds had been reallocated to an unbudgeted project. Like the issue noted in paragraph 4.3.2, this applies to projects that are under $300,000. Failing to cancel pending projects increases the likelihood that capital dollars will be spent more than once for projects that are either unbudgeted or are experiencing cost overruns.

4.3.5 **Recommendation:** Pending projects should be monitored. Working closely with their budget coordinators, the head of each Business Unit has ultimate accountability for ensuring that a Business Unit does not over commit its annual capital budget. If it becomes reasonably certain that a pending project will not materialize or the funds set aside for the pending project have been reallocated to an unbudgeted or over budgeted project, the project should be changed to 'cancelled' status. A change to the Authorization for Investment Proposal (AIP) requires the Budget Coordinator's signature. This signature attests that sufficient funds are available for the capital project.

APPENDIX I

ENGAGEMENT MEMO

From:	Hilbert, Debbie on behalf of Balderson, Carl
Sent:	Monday, November 25, 2002 4:09 PM
To:	Rives, Brad
Cc:	Staffieri, Vic; Aitken-Davies, Richard; Barham, Richard (Powergen); Scott, Valerie; Hudson, Rusty; French, M. Glen; Welsh, Wendy; Hermann, Chris; Thompson, Paul; McCall, John; Vogel, Dave; Smith, Roger (SVP Proj Eng)
Subject:	LEC - Capital Investment Process Audit Engagement Memo

Audit Services has scheduled an audit of LG&E Energy Corp.'s (LEC) Capital Investment Process. The objectives of this engagement are as follows:

- determine that the procedures set forth in the LEC Corporate Capital Policy are consistently followed by the business units;
- determine that project costs are being monitored while the project is active; and
- determine that a post project analysis is conducted to ensure that cost savings and benefits are met.

The scope of the audit will include the following capital projects:

- Projects active between 1/1/00 - 10/31/02; and
- Projects closed between 1/1/02 - 10/31/02.

Field work is scheduled to begin December 9, 2002.

The audit will be performed by Jorene Logan, Senior Financial and Contract Auditor, and Nancy Koziel, Contract Auditor, under the direction of Bob Aemmer, Manager, Financial, Contract, and Energy Marketing Auditing. We look forward to working with you and your staff during this engagement. Please advise Bob by December 4, 2002, if you would like to schedule an opening conference to provide you an opportunity to discuss the audit objectives, scope, and timing; or you may call me with any questions or comments.

Carl

Debbie Shelton
Director of Audit Services
LG&E Building
4th Floor
502-627-4614
502-627-2590 FAX

To: Brad Rives, Chief Financial Officer
Valerie Scott, Controller
Paul Thompson, Senior Vice President Energy Services

Date: February 16, 2005

Subject: Fixed Assets Cycle – Sarbanes-Oxley 404 Assessment

Audit Services, with the assistance of PricewaterhouseCoopers (PwC), completed a review of Sarbanes-Oxley Section 404 Compliance for the Fixed Assets Cycle. The objectives of the review were to:

- ensure completeness and appropriateness of the information recorded in the SAP Management of Internal Controls (MIC) software;
- review internal control documentation (flowcharts and narratives) for completeness and appropriateness; and
- test the overall operating effectiveness and adequacy of internal controls, including but not limited to, required or desired periodic reviews and evaluations thereof, including those under the Sarbanes-Oxley Act of 2002.

The scope included a review of system and internal control documentation and discussions with employees related to Fixed Assets for the year ended December 31, 2004. There are six transactions within this cycle: Maintenance of Master Data, Acquiring Fixed Assets, Depreciating Fixed Assets, Maintenance, Disposing and Retirement of Fixed Assets, and Impairment. Procedures included the steps listed below:

- performing a risk assessment to determine controls to test;
- gaining an understanding of the process and the controls over the process;
- designing and conducting tests over controls;
- evaluating the design effectiveness of controls; and
- determining whether management's documentation accurately reflects the control environment in place.

These procedures do not constitute an audit of internal controls conducted in accordance with the standards of the Public Company Accounting Oversight Board (PCAOB) such as will be performed by PwC and Audit Services in subsequent years. The completion of these additional procedures in subsequent reviews might reveal other matters that will be reported at that time.

CONCLUSION

Based upon the procedures performed and action plans developed; internal controls appear to be appropriate and operating as designed, except as listed below in the Implementation Plan.

RECOMMENDATIONS

The recommendations address retaining evidence, documenting some additional controls that are in place but not listed in the narratives, reviewing certain policies for appropriateness, and removing some controls listed in the narratives that are actually process steps or duplicates.

In addition to the items listed in the Implementation Plan, Audit Services and PwC provided management with a number of documentation suggestions. These revisions will be made in conjunction with other documentation revisions resulting from the currently ongoing Sarbanes-Oxley (SOA) training, provided by the SOA Steering Committee.

Cc: R. A. Hudson, Director, Generation Accounting & Budget
J. J. Logan, Project Manager, Sarbanes-Oxley
M. R. Lockard, PricewaterhouseCoopers
G. S. Watkins, Director, Supply Chain
S. L. Wiseman, Manager, Property Accounting

IMPLEMENTATION PLAN **USAS FI-04-E-C04**

Implementation Meeting: Phone calls, e-mails, and discussions **Present:** Management: S. L. Wiseman, R. A. Hudson
Date: Various Audit Services: W. A. Zoeller

Recommendations	Agreed/ Not Agreed	Management Action Plan	Person Responsible	Date to be Completed	Management's Follow-up Comments / Date
C.04.07.00.01[1] Audit Services recommends removing from SAP MIC and documentation controls that are actually process steps.	Agreed	Management will remove the identified controls from SAP MIC and documentation as appropriate.	R. A. Hudson	2/28/05	Implemented
C.04.00.00.01 Audit Services recommends that evidence to support the operating effectiveness of the controls for the acquiring fixed asset process be retained.	Agreed	Appropriate evidential documentation will be retained.	S. L. Wiseman	3/31/05	
C.04.02.00.04 Audit Services recommends removing controls that are referencing other controls. By referencing these other controls duplicate/overlapping controls exist within SAP MIC.	Agreed	Management will remove the identified controls from SAP MIC as appropriate.	S. L. Wiseman	2/28/05	Implemented

[1] The issue numbering convention is C.00.00.00.00 with the first two numbers indicating the cycle number, the second two numbers indicating the transaction, the third two numbers indicating the sub-process, and the last two numbers indicating the control activity.

Recommendations	Agreed/ Not Agreed	Management Action Plan	Person Responsible	Date to be Completed	Management's Follow-up Comments / Date
C.04.00.00.02 Audit Services recommends that review and approvals for the depreciating fixed assets and maintenance process be evidenced through signatures and initials.	Agreed	Appropriate evidential documentation will be retained.	S. L. Wiseman	3/31/05	
C.04.02.00.01 Audit Services recommends that controls supporting the selection of depreciation rates be documented and strengthened.	Agreed	Work Order Analysis Checklist, which includes a step to review the selected category / plant account (which corresponds to the depreciation rate) will be periodically reviewed and reperformed by the Manager of Property Accounting or designee. Additionally, the documentation will be updated to reflect this process.	S. L. Wiseman	3/31/05	Implemented
C.04.04.00.01 Audit Services recommends documenting the System Restoration process that is currently in place.	Agreed	Property Accounting will appropriately indicate a System Restoration project on the Work Order Analysis Checklist. Additionally, the documentation will be updated to reflect the manner in which System Restoration projects are handled.	S. L. Wiseman	3/31/05	

Recommendations	Agreed/ Not Agreed	Management Action Plan	Person Responsible	Date to be Completed	Management's Follow-up Comments / Date
C.04.02.00.03 Audit Services recommends capital expenditures that exceed the original Authorization for Investment Proposal (AIP) amount by 10 percent or $100,000 (minimum $25,000) be monitored and reconciled with actual expenditures and revised AIPs are issued and reauthorized.	Agreed	Work Order Analysis Checklist, which includes a step to obtain the revised AIP, will be periodically reviewed and reperformed by the Manager of Property Accounting or designee.	S. L. Wiseman	3/31/05	Implemented
C.04.02.00.02 Audit Services recommends adding a control to ensure positive confirmation is received from all budget coordinators for projects with no activity for 90 days or more. This will help ensure that projects are appropriately unitized or remain in Construction Work in Progress.	Agreed	Manger of Property Accounting will request the budget coordinators to return positive confirmation on the status of the projects with no activity for 90 days.	S. L. Wiseman	3/31/05	

Audit Services

USAS Report No. FI05E295

About:

LG&E Energy LLC

Review of:

Investment Controlling – Joint E.ON Audit

LG&E Energy LLC – Audit Services
Investment Controlling – Joint E.ON Audit
FI05E295

Subject of audit: Investment Controlling – Joint E.ON Audit

Audit location: LG&E Energy LLC (LEL)

Auditors: H. L. DiEnno; R. C. Aemmer

Date of Audit report: October 31, 2005

Report number: FI05E295

Distribution:

Senior Vice President, Corporate Audit (E.On AG)	Dr. M. Holtmann
Chief Executive Officer (LEL)	V. A. Staffieri
Chief Financial Officer (LEL)	S. B. Rives
Director, Corporate Planning and Development	C. Landsmann
Director, Financial Planning and Controlling	L. E. Bellar
Manager, Financial Planning-Corporate	L. M. Hennekes
Manager, Financial Planning-Utility Operations	V. L. Strange
PricewaterhouseCoopers (PwC)	M. R. Lockard

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1 Management Summary

1.1 Main Findings

The results of this audit indicate that LG&E Energy LLC (LEL) maintains general compliance with Company policies and procedures, and guidelines through the monitoring and oversight by LEL's Financial Planning and Controlling Department. These policies and procedures include, but are not limited to, the LEL Capital Policy.

1.2 Assessment of Audit Objectives

The main objectives of the audit were to assess relevant LEL guidelines, management organization, and policies; and review the LEL investment controlling process.

Audit Services conducted interviews and selected a sample of capital projects to review. Based on the procedures performed, Audit Services determined that LEL has guidelines and policies in place to appropriately manage the Investment Controlling process.

1.3 Significant Findings and Recommendations

There are no local recommendations resulting from this audit. However, it is anticipated that some group-wide recommendations for group-wide practices may result from the E.ON Joint Audit review process.

This audit report was discussed with the responsible Managers and Directors of the departments interviewed.

2 Subject of Audit

Basic information on External Consulting Services

The Property Accounting Department maintains guidelines for Investment Controlling. Requirement documentation is located on the Property Accounting intranet website. All departments interviewed use these guidelines.

Slight modifications were made to the protocol that was provided by E.ON to perform this assessment. The modifications included tailoring for appropriate language or activities that reflect the current operations in place. The protocol was completed for each interviewed department, then summarized within the attached protocol in Appendix I.

The audit was based on interviews with LEL personnel, documentation review and evaluation, and testing. Personnel within LG&E Power Services and LG&E Power Incorporated were not interviewed as part of this audit. Those specifically interviewed were:

- Director, Financial Planning and Controlling
- Manager, Corporate Financial Planning
- Manager, Utilities Financial Planning
- Manager, Property Accounting
- Manager, Energy Services Financial Budgeting
- Manager, WKE Accounting
- Team Leader, Distribution Budgeting

3 Detailed report

There are no recommendations resulting from this audit. A brief summary of the findings for each section of the protocol are detailed below.

Section 1 - Guidelines and Instructions

A Capital Policy exists at the LEL level for planning, budgeting, and reporting capital projects. The guidelines have been distributed to appropriate personnel; are maintained on the Company's intranet website; and are consistently and appropriately applied.

Section 2 – Planning
Various strategy meetings occur between E.ON and LEL. LEL issues planning guidance to the business unit leaders and other key planning contacts. The individual Medium Term Plans (MTPs) and Capital Plans are developed by the business units, then rolled into one LEL MTP and Capital Plan. Meetings are held by business units and at an overall level on a regular basis to ensure that projects continue to align with strategic goals. This process is performed in accordance with the guidelines stated in E.ON's Reporting Manual.

Section 3 - Budgeting
The multi-year Capital Investment Plan is used to inform senior management of future capital spending projections. These plans are prepared annually on an operating business unit basis and include the budget of capital projects during the annual planning period. The first year of the capital investment plan, once approved, becomes the formal budget for that year. All capital spending expected during the year must be budgeted. Although individual projects are approved during the budgeting process, they must also be approved and proper signature approval obtained before the capital project begins. This process is performed in accordance with the guidelines stated in the LEL Capital Policy.

Section 4 - Reporting
Capital projects are reported to various committees based on certain criteria. Projects are reported on an overall level in monthly management and performance reports, monthly analyses, and quarterly analyses. Reports on individual projects are generated monthly to provide information on spending, forecasts, and comparisons to budget. The Company appears to have appropriate and sufficient reporting mechanisms in place.

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4 Appendix I – Protocol Summary

No.	Question	Response
A	**Guidelines, Rules, Instructions**	
	Existing Guidelines/Rules	
1	Are there articles of corporation/business rules/rules of procedure?	Yes, investment guidelines (the LEL Capital Policy) exist at the LEL level for planning, budgeting, and reporting capital projects. The guidelines have been distributed to appropriate personnel and interviewed departments were aware of, and in compliance with, the guidelines. The guidelines are maintained on the Company's intranet website.
2	E.ON Planning and Controlling Manual	The Company is aware of and follows the E.ON Planning and Controlling Manual. The LEL Capital Policy complies with the E.ON Planning and Controlling Manual.
3	Are there guidelines on planning, budgeting and reporting, and investment guidelines?	Yes, investment guidelines (the LEL Capital Policy) exist at the LEL level for planning, budgeting, and reporting capital projects. The guidelines have been distributed to appropriate personnel and interviewed departments were aware of, and in compliance with, the guidelines. In addition, approval guidelines exist in the Investment Decision Procedure-Investment Approval Limits Matrix (ALM). The guidelines are maintained on the Company's intranet website.
4	Are there project management guidelines, including project organization, project reporting, project review, and final costing?	Yes, investment guidelines (the LEL Capital Policy) exist at the LEL level for project management guidelines. The guidelines have been distributed to appropriate personnel and interviewed departments were aware of, and in compliance with, the guidelines. The guidelines are maintained on the Company's intranet website.
5	Are there instructions for handling associated companies?	Yes, associated companies are covered by the LEL Capital Policy.

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No.	Question	Response
6	Are approval processes documented according to the steps actually performed?	Yes, the approval process is accurately documented according to the steps performed in the LEL Capital Policy and the authority limitations set forth in the Investment Decision Procedure-Investment Approval Limits Matrix (ALM). There are various levels of approvals. IT projects greater than $250,000, non-IT projects greater than $1,000,000, and development projects greater than $500,000 are brought before the Investment Committee for approval. All projects greater than $300,000 must have a business proposal, capital evaluation model, and must be approved by the Financial Planning Department.
7	Does the approval process govern situations when the originally approved budget is exceeded?	Yes, the LEL Capital Policy provides guidelines on the approval process when the originally approved budget has been exceeded. When it is apparent that the amount originally approved will be insufficient (project is expected to be ten percent or $100,000 over; whichever is less, subject to a minimum of $25,000) to complete the project, a revised Authorization for Investment Proposal (AIP) must be completed. The additional funding requested must be offset by a like reduction in one or more budgeted projects or the additional funding requires prior written approval by the CFO and CEO.
8	Are there rules regarding minimum expected useful life?	Yes, there are rules regarding minimum expected useful life. Although not explicitly stated in the LEL Capital Policy, the LEL Capital policy does state that “the Controller will have the ultimate authority of interpreting expense versus capital decisions based on generally accepted accounting principles (GAAP)". GAAP policy states that assets with a useful life less than one year are expensed and this policy is followed by the Company.
9	When do projects need supplementary review?	Projects are approved in accordance with the ALM. Investment Technology projects greater than $250,000 and all other projects greater than $1,000,000 must be approved by the Investment Committee. All projects greater than $300,000 must have a business proposal, capital evaluation model, and must be approved by the Financial Planning Department.

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No.	Question	Response
	Alteration of Guidelines/Rules	
10	Are formalized procedures implemented?	Per the Policy Development, Approval, and Compliance Policy, changes to policies and approvals must go through the appropriate channels and ultimately be approved by the CFO.
11	Who initiated the last alterations?	Property Accounting initiated the last alterations.
12	Do communication channels for alterations exist?	Yes. Alterations are properly communicated to those affected before being approved. Once approval is obtained from affected parties and the CFO, the policy is shared with affected departments and on the Company intranet.
13	Are alterations communicated in a timely manner?	Yes.
B	**Planning**	
	Strategy Planning	
14	Date and topic of last strategy meeting?	The last strategy meeting was a strategy roundtable organized by E.ON Corporate Development. This meeting was held in August. The last meeting of the Investment Committee was held on 8/12/05 to approve capital projects. The last meeting of the LG&E Resource Allocation Committee (LRAC) was held on 9/13/05 to prioritize projects.
15	Are minutes of this meeting available?	Meeting minutes are kept and available for Investment Committee meetings. E.ON is responsible for minutes for the meetings it organizes.

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No.	Question	Response
16	How was the output/were the results of the MU and E.ON strategy meetings realized or forwarded?	Various strategy meetings occur between E.ON and LEL. LEL issues planning guidance to the business unit leaders and other key planning contacts. The individual MTPs and Capital Plans are then developed by the business units. They are reviewed by the business unit leaders and are then presented to LEL Controlling for approval. Once approved, the individual MTPs and Capital Plans are rolled into one LEL MTP and Capital Plan.
17	How is it ensured that the strategy goals are realized on MU and BU level?	The LRAC reviews company projects and reprioritizes on a company level based on input from each business unit and in conjunction with the market unit and business unit strategies.
18	How are investment decisions prioritized?	Business units decide which investments to include in the Capital Plan. This plan is then approved by the senior officers. Once the plan has been approved and is in place, projects continue to be prioritized as the Capital Plan is carried out by the LRAC. The LRAC maintains a database of the last ten percent of capital projects in the Capital Plan and the first ten percent of proposed capital projects that did not make it into the Capital Plan. These projects are then grouped into general categories. The committee decides if a category will have dollars added or subtracted. The business unit decides on an individual project level which should receive the cutback or added dollars.
19	Which specified targets were stipulated for concrete investment decisions, e.g. regarding EBIT, DCF?	Specific targets for investment decisions include Discounted Cash Flows (DCF), Return on Capital Employed (ROCE), Internal Rate of Return (IRR), Internal Operating Profit (IOP), and Earnings Before Income Tax (EBIT). These targets are specified in the LEL Capital Policy and in the Capital Evaluation Model (CEM).
	MTP, Capex Plan	
20	Realization in accordance with guidelines?	Yes, the Medium Term Plan (MTP) and Capital Plan are developed in accordance with guidelines established by the Company and E.ON. The capital plan is part of the MTP.

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No.	Question	Response
21	Initiation	The MTP and Capital Plan process is governed by E.ON timelines. The MTP process begins when LEL planning guidance is issued to the business based on strategy meetings held between E.ON and the market units. The process typically starts in April or May.
22	Time schedule	Once the planning guidance has been received, the business units start developing their MTP and Capital Plan. The plans are completed in June or July and are then reviewed by the senior business unit leaders. In July or August, the plans are presented to LEL for approval. Once approved, the plans are rolled into one LEL MTP and Capital Plan during September. In October, the plan is submitted to E.ON for review.
23	Completion	In November, the plan is presented to the E.ON management board. Based on any changes determined during the E.ON board review, final adjustments to the plan are made. The final plan is distributed to senior officers.
24	How is the Capex plan checked and verified?	The Capital Plan is checked and verified through the review process by business unit leaders and Financial Planning. The plan is developed by each business unit and once finalized is sent to the budgeting group. There are various levels of review and approval. It is ultimately approved by the CEO and is then sent to E.ON for review and approval. The plan is checked and verified throughout the year by monthly review of budgeted to actual spending, as well as monthly meetings to discuss and reprioritize projects.
25	Are financing aspects on the next higher level taken into account for individual projects with borderline profit?	Yes. Each business unit develops a Capital Plan. The plan is reviewed and approved and is rolled up into the overall Capital Plan. Individual projects are reviewed in detail by the Financial Planning Department and the Investment Committee when they meet certain criteria. All projects follow these guidelines, including those with borderline profit.

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No.	Question	Response
26	Does the overall Capex plan correspond with the individual planning of the business or divisions? How is this ensured?	The overall Capital Plan corresponds with the individual planning of the business units. The business units develop their own plan. Individual plans are reviewed and approved by business unit leaders before being submitted to LEL. The plans are then reviewed and approved by the Financial Planning department. Once approved, LEL rolls the individual plans into one plan. The overall plan is reviewed and approved by senior officers and is then submitted to E.ON for final approval.
27	Is the strategic allocation of individual projects and their prioritization understandable?	Yes, the allocation and prioritization of individual projects is understandable. The LRAC meets monthly to prioritize projects. This committee is developing a charter. Guidelines for prioritization are included in this draft charter.
28	Which targets were set by the next higher level? Were they realized?	In the initial stages of planning, the targets are given to the business units to include in their budget. The targets were realized in Fiscal Year 2004.
29	On which data is the MTP based (i.e., figures drawn from past experience, quality/quantity assured data, detailed bottom up planning)	The MTP is based on bottom up planning.
30	Is inflation taken into account (based on the E.ON prognosis group?)	Yes. The E.ON inflation rates are provided to the business units who include it in their plan. This information is provided in the LEL planning guidance distributed to the business units.
31	Do project results have an impact on the MTP (i.e., delay, cost increase)	The company reforecasts once it is in the year that was budgeted. If a project is delayed or there is a cost increase, the forecast is changed. This is performed on a monthly basis and reforecasts are sent to E.ON quarterly. Reforecasts are reviewed by the Financial Planning department. This procedure is in accordance with E.ON's Planning and Controlling Manual.

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No.	Question	Response
32	Is MTP/budget for current year compared with figures from last year? (especially regarding not realized pro-jects)	Yes, the MTP/budget for the current year is compared to the prior year MTP/budget. Not realized projects are due to shifting timeframe or shifting priorities. Projects that are not realized are reported in the monthly management reports through the budget to actual comparison.
33	How are subsidiaries in-cluded? Does the current MTP equal the sum of all individual MTPs?	Subsidiaries are rolled up into the overall plan. The current MTP equals the sum of all individual MTPs.
C	**Budgeting**	
	Budgeting on Company Level	
34	Realization in accordance with guidelines?	Yes, the MTP and Capital Plan are developed in accordance with guidelines estab-lished by the Company and E.ON. The first year of the MTP becomes the budget for the current year.
35	Initiation	The Budget process is an ongoing process. It typically starts in April or May and is finalized in October or November. See items above 20-23.
36	Time schedule	The Budget process is an ongoing process. It typically starts in April or May and is finalized in October or November. See items above 20-23.
37	Completion	The Budget process is an ongoing process. It typically starts in April or May and is finalized in October or November. See items above 20-23.

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No.	Question	Response
38	Are the budget figures in 2005 in line with the Capex plan for 2005-2007?	Yes. The multi-year Capital Plan is used to inform senior management of future capital-spending projections. These plans are prepared annually on an operating business unit basis and include the forecast of capital projects during the annual planning period. The first year of the capital investment plan, once approved, becomes the formal budget for that year.
39	Which extraordinary measures (buffers) are foreseen in the budget (amount, type, etc)?	Ten percent contingencies are included for some projects; however, this is on a case by case basis and does not apply to all projects. Contingency amounts are clearly identified on the AIP. The AIP is reviewed and approved in accordance with the ALM.
40	Extraordinary investments in relation to total budget	High dollar projects were approximately 22 percent of the 2005 budget.
41	Supplementary approvals in relation to total budget	The approval process is the same for all projects during the budget process.
42	How is the approval of extraordinary investments handled when the total investment amount is limited or frozen?	The investment is submitted to the Investment Committee for additional approval.
43	Were plausible reasons for these extraordinary measures given?	Yes, plausible reasons must be given for extraordinary measures.
44	Are all planned investments included in the budget?	As required by the LEL Capital Policy, all capital spending that is expected to occur during the year must be budgeted in the current year commitment. The budget is reviewed by the business unit leaders and by the Financial Planning Department to ensure that all planned investments are included in the budget.

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No.	Question	Response
45	Does the non-individualized part of the budget (aggregated figures for smaller projects) include coherent measures of considerable amount?	The company prepares detailed budgets for all projects. All projects are reviewed by the individual business units. Larger projects receive additional levels of review.
46	Are all measures of the subsidiaries included? How is this ensured?	Yes. Each business unit submits a capital plan to be rolled into the overall plan. Once the individual plans have been summarized, the total amount budgeted is agreed to the total cash flow for capital expenditures.
47	Are possibly unspecified measures/funds included?	There are no unspecified funds.
48	Number of individual projects requiring approval per approval level?	All projects must follow the ALM for approval at the appropriate level.
49	Was the budget approved? When?	Yes, The 2005 budget was approved by E.ON November 17, 2004.
50	Is the financial demand for investments determined or adjusted during the budgeting process?	Yes. If necessary, financial demand is shifted between projects in the budget. These adjustments are determined during LRAC meetings.
	Project Planning-Adherence to guidelines/rules	**The following sub-section refers to testing attributes for specific items tested. A sample of eight capital projects was selected for testing. No exceptions were noted.**

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No.	Question	Response
51	Project proposal is complete	Yes. All projects had a completed proposal.
52	Plausible project reason? Is the project coherent with strategic goals?	Yes. A plausible project reason was given for all projects. The reason was coherent with strategic goals.
53	Is the calculation of profitability plausible?	Yes. The profitability calculation was plausible for all projects.
54	According to which criteria is the profitability evaluated?	DCF, ROCE, IRR, IOP, EBIT (See 4.19 above.)
55	Are financial effects considered and additional approvals from next level authorities available? Responsibility for approval?	Yes, financial effects were considered for each project and proper approval was obtained. The approvals followed the ALM.
56	Are payments completely considered?	Yes. Cash outlays and inflows were considered for each project.
57	Which economic lifetime was selected? Is this in line with the operating life of the entire object?	The economic lifetime varied based on the type of capital project. All economic lifetimes were in line with the operating life of the entire object.
58	Is the risk evaluation plausible?	Yes. The risk evaluation was plausible for each project.

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No.	Question	Response
59	Is the repayment period appropriate compared to the risk?	Yes. The repayment period was appropriate compared to the risk for each project.
60	Are effects on the business segments EBIT, ROCE, etc, are described and understandable?	Yes. The effects on the business segments are described and understandable.
61	Investment Volume (estimation, experience, experts knowledge)	Yes, each project considered estimations, experience, and expert knowledge.
62	Are personnel cost included?	Yes. Personnel costs were included for each project.
63	Are overheads included?	Yes. Overheads were included for each project.
64	Are possibly not listed/secret funds available?	Some projects have a ten percent contingency amount included. This amount is clearly defined in the proposal.
65	Time to next MTP well dimensioned?	Yes. There is sufficient time to the next MTP.
66	Are projects belonging together reviewed together as one project?	Yes, projects belonging together were reviewed together as one project.

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No.	Question	Response
67	Was the project included in the MTP of the respective year?	Yes, all projects were included in the MTP of the respective year.
68	Approval over all authorities available?	Yes. Proper approvals were obtained in accordance with the ALM.
D	**Reporting**	
	Capex Control-ling/Reporting	
69	In which form are invest-ments reported to the next higher level? What is the reporting cycle? Are there plausibility checks?	Projects are reported to management in the monthly Management and Performance reports. Plausibility checks, including agreement to the source system and manage-ment review and approval, occur before the reports are distributed.
70	Are figures from associated companies correctly ac-counted? Which reports are received from the sub-sidiaries?	Yes, figures from associated companies are correctly accounted. Capital reporting occurs monthly. Reports from associated companies are rolled up and balanced to the consolidated financial statements. Each business unit prepares a management report.
71	Based on which key figures are the results of the in-vestments viewed and mon-itored?	IOP, IRR, ROCE, EBIT, and DCT (see 4.19 above) are monitored for projects over $300,000. In addition, all projects, including smaller projects, are monitored by budg-et coordinators.

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No.	Question	Response
72	Long term projects: Are initial planning premises regularly checked and is the profitability recalculated where/when necessary? Are these changes reported to the next higher level (especially in connection with earlier referenced projects?)	Major projects are approved in accordance with the ALM and are tracked through monthly management and performance reports. Profitability is recalculated when necessary and changes are reported to the next higher level.
73	Which additional internal controlling reports exist? Are these in line with the reports to the next higher level? Do the separate reports lead to additional work?	On a quarterly basis, the Financial Planning-Utility Operations department produces a Capital Projects Over $500,000 Report, which includes a project to date summary of all approved projects over $500,000. The report shows the current month year to date and the full year forecasted spending compared to budget. Monthly performance and management reports are also distributed that include information on capital projects. The separate reports do lead to additional work.
74	Have steps been taken when target-actual deviations were recognized? Were those measures successful? Are reasons given for deviations?	The capital budget remains the same. If a deviation is needed due to an opportunity or emergency, the projects are absorbed by adjusting the schedule in the overall capital forecast to still meet the total capital budget.
75	Are the figures of the respective reports in line with the aggregated figures of the individual projects? How is this ensured?	Yes, the figures of the respective reports are in line with the aggregated figures of the individual projects. Reports from the Oracle Financial and Material System (OFMS) and JD Edwards are used to balance the financial statements. Property, Plant, and Equipment rollforwards are prepared and are agreed to the cash flow statement. Amounts in reports are agreed to source systems.

No.	Question	Response
	Which systems are used?	
76	How is the unused investment budget marked and is it returned?	Unused investment budget amounts are due to a shift in timing or a shift in priorities. Thus, amounts are moved to the proper time period or a different project due to a shift in priorities.
77	Do the reports also include information regarding the actual project progress? Are project status and delays included in the reporting?	Yes, project progress, status and delays are included in the reports.
78	How many reports need supplementary approval? Were approval limits exceeded?	Management and Performance reports are reviewed and approved by the Financial Planning and Controlling management, Chief Financial Officer (CFO), and Chief Executive Officer (CEO) before being sent to E.ON.
79	How extensive is the complete reporting?	Extensive reporting exists on a project by project basis for every area.
	Financial Planning	
80	Does the long-term financial planning consider the current Capex forecast?	Yes, long-term planning considers the current Capital Plan forecast.
81	Are deviations from planning figures explained in a plausible way?	Yes, deviations are explained in a plausible way.

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No.	Question	Response
82	Are the projects' payment schedules considered in the planning?	Yes, the projects' payment schedules are considered in the project planning.
	Controlling on Project Level	
83	Is there periodic reporting of project status?	Yes. For the business units interviewed as part of Audit Services testing, management reports are distributed that report major capital projects spending, budgeted amount, and forecasted amount. These reports are distributed to management. In addition, reports are generated monthly for each project that compares the approved amount to the actual spending. These reports are distributed to the budget coordinators.
84	Are possible exceedings of budget in next fiscal year monitored and controlled?	The reports noted above are monitored. In addition, the business units interviewed have committees in place that meet monthly to monitor and allocate capital projects.
85	Are all costs accrued on time?	Yes, costs are accrued timely.
86	Is budget exceeding in ERP system possible?	Yes. A project's budgeted amount for the year is entered into OFMS. It is possible for spending to exceed this approved amount. However, the reports and meetings mentioned previously would identify budget overruns.
87	Are additional tools in use (i.e. Excel spreadsheets net to ERP system)	Excel is used primarily for reporting purposes.

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No.	Question	Response
	Reporting on Project Level	
88	Which reports are generated?	In addition to the reports noted above, reports are generated quarterly at the Corporate level that details projects greater than $500,000.
89	What is the reporting cycle?	Most reports are generated monthly; however, some are generated quarterly.
90	Are there appropriate reports for schedule, costs, and progress?	Yes, the above mentioned reports are generated and meetings are held to discuss project details.
91	Is the distribution list appropriate?	Yes, the distribution list is appropriate and is reviewed monthly.
92	Are deviations from budget founded (considered in forecast? Are counteractive measures given?)	Yes. The monthly reports are reviewed to determine any deviations from budget and appropriate follow-up occurs.
93	How are deviations reported? (i.e., Comparison Budget and YTD)	Deviations are reported through the monthly management reports, which includes budget to actual comparisons.
94	Are deviations greater than 10% reported to the next level divisions? Are Exceeding reported to E.ON where applicable (authority limits)?	Yes. Projects that exceed budget by ten percent (minimum $25,000), or $100,000, are sent back to the project proponent for additional review. Items are reported to E.ON where applicable.

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No.	Question	Response
95	Are post approvals applied in time?	Yes, post approvals are applied timely.
96	Are profitability calculations updated where applicable?	Yes, if applicable.
97	Are updated forecasts considered in the financial planning?	Yes, updated forecasts are considered in the financial planning.
98	Are there any post completion audits? Post calculations? Who is setting up post analysis?	Yes. As required by the LEL Capital Policy and the Investment Review Policy, all projects that go before the Investment Committee receive a post-implementation review.
	Capitalization and Depreciation	
99	Which depreciation was chosen? Are there any special depreciation rates?	For the utilities, depreciation rates are chosen based on a depreciation study that is performed at the Company. Projects are depreciated based on the account they belong to. For WKE, depreciation rates are determined based on the estimated useful life projected by the plant manager.
100	Update of depreciations due to change of lifetime?	Updates are made during the depreciation study for the utilities, if necessary. Updates are also made, if necessary for WKE.
101	Capitalization of fixed assets regulated?	Yes. Fixed assets are capitalized according to the depreciation study based on the assets economic life and are capitalized according to GAAP.

Audit Services

Audit Report No. FI07E335

E.ON U.S. LLC

International Accounting Standards Conversions

Date Issued: December 3, 2007

E.ON U.S. LLC Audit Services
International Accounting Standards Conversions Audit
FI07E335

Reviewed Departments:	Regulatory Accounting & Reporting and Property Accounting
Subject of Audit:	International Accounting Standards Conversions
Auditor(s):	S. Segbers, R. H. Dowdell
Reviewers:	R. C. Aemmer, D. A. Shelton
Fieldwork Completed:	August 28, 2007
Draft Report Issued:	October 28, 2007
Final Report Issued:	December 3, 2007

To:

Controller	V. L. Scott

CC:

Chief Executive Officer	V. A. Staffieri
Chief Financial Officer	S. B. Rives
Senior Vice President, Corporate Audit (E.ON AG)	Dr. M. Holtmann
Director, Utility Accounting & Reporting	S. L. Charnas
Manager, Property Accounting	S. L. Wiseman
Manager, Regulatory Accounting & Reporting	M. M. Kelly
Manager, Corporate Accounting	C. M. Garrett
PricewaterhouseCoopers (PWC)	L. A. Prather
PricewaterhouseCoopers (PWC)	A. L. Boyd

1 Management Summary

1.1 Introduction

1.1.1 Audit Services (AS) has completed an audit of the conversions from E.ON U.S. LLC's (EUS) United States - Generally Accepted Accounting Principles (US-GAAP) based financial statements to International Financial Reporting Standards (IFRS) based financial statements. The objectives of this engagement were to ensure:

- adjustments from US-GAAP figures to IFRS figures are calculated / performed correctly; and
- calculation methods applied are conceptually in line with IFRS requirements.

1.1.2 Audit procedures included a review of policies, procedures, and conversion methodologies applied; and re-calculation and review of adjustments performed.

1.1.3 The scope of the audit was limited to conversions performed for Louisville Gas & Electric Company (LG&E) and Kentucky Utilities Company (KU). The audit scope was further limited to focus on Regulatory Assets and Liabilities, Asset Retirement Obligations (ARO), and Capitalized Interest.

1.2 Conclusion

1.2.1 Audit Services reached the following conclusions;

- the underlying methodology and the actual calculations related to the Regulatory Assets and Liabilities are reasonable,
- the underlying methodology of the ARO adjustment calculations is also reasonable,
- the computations regarding capitalized interest are sound, and
- the treatment of capitalized 'Allowance for Funds used during Construction' (AFUDC) for IFRS purposes exhibits potential for adjustment.

1.2.2 No Internal Control System findings were identified in this review.

1.3 Main Findings and Recommendations

1.3.1 Audit Services recommends that the equity component of AFUDC capitalized under US-GAAP jurisdiction be excluded from the IFRS calculation basis of Capitalized Interest and that further AFUDC reversal entries may be made. Additionally, Property Accounting should consider materiality if making any IFRS ARO inflation adjustments to appropriate KU assets.

1.3.2 For a complete list of recommendations and management action plans, see Appendix 1.

2 Background

2.1 Overview

2.1.1 E.ON AG will prepare its first consolidated IFRS financial statements as defined by IFRS 1 as of December 31, 2007. The effective date of E.ON AG's IFRS consolidated opening balance sheet was January 1, 2006 (date of transition) due to the requirement to provide comparative figures for the year 2006. The first quarter of 2007 was the first published IFRS E.ON AG interim report.

2.1.2 As EUS is a part of E.ON AG's consolidation basis, it must provide E.ON AG with financial statements in accordance with IFRS beginning January 1, 2006. EUS created IFRS adjustment companies (i.e., company 700 for LG&E) to hold any IFRS adjustment entries. EUS' IFRS financial statements are then derived from the US-GAAP company accounts (i.e., company 100 for LG&E) modified by the IFRS adjustment companies accounts.

2.1.3 The responsibility for performing the IFRS conversions includes various departments within EUS.

3 Detailed Report

3.1 Regulatory Assets and Liabilities

3.1.1 Regulatory Assets and Liabilities recognized in EUS' US-GAAP financial statements are based on principles prescribed in the Statement of Financial Accounting Standards (SFAS) No. 71 'Accounting for the Effects of Certain Types of Regulation'. SFAS No. 71 allows utilities to establish regulatory assets for incurred costs which will be recovered in the future and liabilities for current recovery of costs which are expected to be incurred in the future. IFRS does not contain a comparable standard. IFRS requires the revenues and expenses subject to special treatment under SFAS No. 71 to be recognized immediately in the income statement. Thus, the corresponding US-GAAP journal entries are reversed for IFRS reporting purposes.

3.1.2 For a sampled set of June 2007 journal entries affecting Regulatory Assets and Liabilities under US-GAAP jurisdiction, AS verified the reversal through the corresponding IFRS adjustment journal entries. Regarding LG&E, AS reviewed the journal entries affecting the Fuel Adjustment Clause (FAC) asset, the Gas Supply Adjustment asset, and the Accumulated Cost of Removal liability. Concerning KU, AS verified the reversals of the US-GAAP journal entries relating to the FAC asset, the Spare Parts liability, and the Rate Case Expense asset. The IFRS adjustment entries made by EUS entirely reversed the corresponding US-GAAP entries and ensured an immediate recognition of the related revenues and expenses in the IFRS income statements. No exceptions were noted.

3.2 Asset Retirement Obligations (ARO)

3.2.1 Audit Services analyzed the assumptions underlying the ARO asset and liability calculations arising under US-GAAP for both LG&E and KU. AS agrees with the assumptions applied by Property Accounting.

3.2.2 The accounting treatments of ARO under US-GAAP and IFRS exhibit few but significant differences. Those differences are;

- the interest rate used to discount the ARO liabilities and assets to their present values (PV), and whether revisions to the interest rate need to be accounted for (as is the case under IFRS[1]),
- the recognition of a regulatory asset under US-GAAP accounting, in contrast to IFRS, to offset the income statement effects of the depreciation of ARO assets and the accretion of ARO liabilities (due to SFAS No. 71),
- the IFRS recognition of a provision for ARO due to legal and constructive obligations, and
- the International Accounting Standard (IAS) 37 'Provisions, Contingent Liabilities, and Contingent Assets' states that 'if some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognized as a separate asset when, and only when, it is virtually certain the reimbursement will be received if the enterprise settles the obligation'.

3.2.3 Due to the conceptual differences between the treatment of an ARO under US-GAAP and IFRS, it is EUS' policy to reverse all related ARO US-GAAP journal entries before recording the ARO amounts for IFRS purposes. AS verified that KU's IFRS adjustment entry for June 2007 fully reversed the US-GAAP entry. Thus, the US-GAAP ARO effects were entirely reversed for IFRS reporting purposes. No exceptions were noted.

3.2.4 The IFRS adjustment entry is manual and susceptible to error. Therefore AS assessed whether the amounts calculated for the IFRS' ARO amounts agree with the journal entry for KU for the period of June, 2007. No exceptions were noted.

[1] IAS 37 requires the use of a discount rate that reflects the current market assessment of the time value of money at each balance sheet date and thus, calls for a re-measurement of the liabilities whenever the discount rate at a given balance sheet date changes. Adjustments arising from changes in the current discount rate are added or deducted from the cost of the related asset.

3.2.5 The Excel spreadsheets used to calculate the ARO asset and liability values, adjustments arising from interest rate revisions, and any resulting depreciation / accretion expenses were reviewed. AS agrees with the methodology applied by EUS with respect to the technical computational approach chosen to determine the ARO amounts for IFRS reporting purposes.

3.2.6 At 12/31/2006 EUS performed the calculations necessary to adjust the ARO liabilities and assets due to a revision in the interest rate. These calculations called for an adjustment of both the ARO liabilities and assets at the same amount as the liability adjustment drives the asset adjustment. EUS correctly calculated the overall adjustment resulting from the interest rate components for the liability-side and adjusted the ARO liabilities, bringing them to their correct book value at 12/31/2006.

3.2.7 EUS made revisions to correct for three periods left out in the initial inflation adjustment of the ARO amounts (years 2003 – 2005). The adjustment to make up for the missed periods in the initial inflation calculation required adjustments to the ARO liabilities and assets at different amounts.[2] EUS, however, adjusted the ARO asset by the same amount as the ARO liability. EUS should have performed an additional calculation separate from the liability calculation to determine the proper adjustment to the asset-side amounts resulting from the original incomplete inflation calculation. This led to a misstatement of the ARO assets, however it has not been quantified at this time. The adjustment for the missed periods in the initial inflation adjustment was performed for LG&E but not for KU.

3.2.8 **Recommendation:** Management should determine the overall impact of correcting the missed period data for KU, and the ARO asset calculations for LG&E and KU performed at 12/31/2006. Any further procedures should be based on materiality.

3.2.9 Audit Services verified that EUS is not subject to constructive obligations with respect to ARO as the Property Accounting Department Manager confirmed its interpretation with E.ON AG. No exceptions were noted.

3.2.10 Audit Services verified that EUS has not received any reimbursements which would qualify under IAS 37. No exceptions noted.

[2] In order to determine the right adjustment amounts for the ARO assets and liabilities due to the missed inflation periods, the deltas between what would have been the correct values of the assets and the liabilities and the actual values (as determined by EUS) of the assets and liabilities at 12/31/2006 needed to be considered before any adjustment due to the interest rate revision at that date. These deltas differ in part to the initial calculation methods of the ARO assets and liabilities prescribed by the first time adopter exemption. Once the ARO assets and liabilities had been brought to their correct net book value at 12/31/2006, they would have been ready for adjustment due to the interest rate revision at the same amount.

3.3 Capitalized Interest

3.3.1 According to SFAS No. 34 'Capitalization of Interest Cost', US-GAAP establishes standards for capitalizing interest expense as part of the cost of an asset. SFAS No. 71, however, allows LG&E and KU to expense all interest related to Kentucky operations because 'Construction Work in Progress' (CWIP) is included in the rate base. This does not apply to non-Kentucky jurisdictional AFUDC. IAS 23 'Borrowing Costs' states that borrowing costs related to a 'qualifying asset' should, under certain conditions, be capitalized as part of the cost of an asset. IAS 23 further states that if funds have not been specifically borrowed for the acquisition or construction of a 'qualifying asset', the capitalization rate will be the weighted average of the borrowing costs applicable to the general pool of borrowings.

3.3.2 The IFRS journal entry related to Capitalized Interest is a manual entry. AS agreed the calculated interest and the amount of depreciation expense with the amounts posted in the IFRS adjustment entry. No exceptions were noted.

3.3.3 Once the construction or acquisition of a 'qualifying asset' is completed, both the asset and the capitalized interest for the asset are re-classified from the CWIP to a fixed asset account and depreciated normally. AS reviewed the June 2007 IFRS depreciation expense calculation of the capitalized interest components of the Ghent 3 FGD and SCR assets and supports the technical computational approach chosen by EUS.

3.3.4 IAS 23 paragraph 17 states that 'the amount of borrowing costs capitalized during the period should not exceed the amount of borrowing costs incurred during that period.' EUS maintains an excel spreadsheet that prevents any violation to this requirement of IAS 23.17. No exceptions were noted.

3.3.5 To determine any current period's amount of interest to be capitalized for a project, EUS calculates the average of the current and prior period's CWIP balances and applies the capitalization rate to this average. Under US-GAAP/Federal Energy Regulatory Commission (FERC) jurisdiction, any capitalized AFUDC charge is included in this balance. To use the US-GAAP CWIP balance for IFRS purposes, EUS subtracts the AFUDC from the CWIP balance. Based on AS review of the Ghent 3 Flue Gas Desulphurization (FGD) project, the debt component of the capitalized AFUDC is subtracted while the equity component is not. This incorrectly increases a given period's IFRS CWIP balance and the calculation basis of the amount of interest to be capitalized.

3.3.6 IFRS does not recognize AFUDC included in CWIP. AFUDC inclusion in CWIP is a FERC requirement. EUS had not reversed capitalized AFUDC for any non-qualifying asset[3]. The capitalized AFUDC amounts for these non-qualifying assets were included in the IFRS financial statements, which may lead to an overstatement of these assets by the non-reversed amount of AFUDC.

3.3.7 As indicated in 3.3.6 and due to the conceptual similarity of US-GAAP/FERC AFUDC and IFRS Capitalized Interest, EUS made the decision to reverse capitalized AFUDC only for assets that qualify for interest capitalization under IFRS and that exceed the E.ON AG threshold. In practice, EUS reverses only the debt component of the AFUDC 'qualifying assets' exceeding the threshold. The equity component of such assets is not reversed. The inclusion of the equity component causes the amount of capitalized interest recognized for IFRS reporting purposes to be overstated during the construction periods and, upon completion and re-classification, to the respective fixed asset account (capitalized interest on Ghent 3 FGD is therefore overstated by an amount of approximately $500,000).

3.3.8 **Recommendation:** For IFRS reporting purposes, EUS should reverse the entire amounts of AFUDC (debt and equity components) capitalized under US-GAAP/FERC jurisdiction for both qualifying and non-qualifying assets. This would ensure compliance with the requirement to recognize capitalized interest only for assets that a) meet the IFRS requirements for interest capitalization and b) exceed the threshold set by E.ON AG and avoid misstatements.

[3] A non-qualifying asset either does not meet the IFRS recognition criteria or does not exceed a threshold of 50 million Euros as set by E.ON AG upon adoption of IFRS

Ref.	Recommendations	Management Action Plans	Person Responsible	Date to be Completed	Follow-Up
3.2.8	EUS should analyze the effect and materiality of correcting the missing period data used in the 12/31/2006 ARO calculations as well as any adjustments to the ARO assets calculations performed at 12/31/2006. Any further procedures should be based on the materiality of the overall effect. Note – These calculations and adjustments should be made based upon materiality. All calculations and assumptions should be documented and the documentation retained should future discussion be necessary.	Property Accounting Department will continue to research and discuss the findings with E.ON Corporate Center. A decision will be made before the end of the year regarding any corrections to be made. All supporting documentation necessary for the decision will be retained.	S. L. Wiseman	January 8, 2008; within the December year end closing process	
3.3.8	For IFRS reporting purposes, EUS should reverse the entire amounts of AFUDC (debt and equity components) capitalized under US-GAAP/FERC jurisdiction. This would ensure compliance with the requirement to recognize capitalized interest only for assets that a) meet the IFRS requirements for interest capitalization and b) exceed the threshold set by E.ON AG and avoid misstatements.	The recommendation will be implemented beginning with the September 2007 financial period.	S. L. Wiseman	November 30th, 2007	Completed during October 2007 close, early in November 2007.

US AUDIT SERVICES

LG&E ENERGY CORP.
REPORT NO. USAS IS-02-E-155

AUDIT REPORT

LG&E ENERGY CORP.

SUPPLY CHAIN

E-PROCUREMENT AUDIT

Date Issued: March 10, 2003

LG&E ENERGY CORP. AUDIT REPORT No. USAS IS-02-E-155

LG&E ENERGY CORP
SUPPLY CHAIN

E-PROCUREMENT

CONTENTS

Audit carried out by: L. H. Buckner, D. A. Shelton
Report reviewed by: C. A. Balderson

Field Work Completed	11/12/02
Draft Report Issued	11/26/02
Final Report Issued	03/10/03

Circulation List

W. C. Welsh	Senior Vice President, Information Technology
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V. L. Scott	Director, Financial Planning and Accounting, Utility Oper.
G. S. Watkins	Director, Supply Chain

Executive Summary
PwC External Auditors

Synopsis
Audit Committee

1 EXECUTIVE SUMMARY

1.1 Introduction

1.1.1 Audit Services recently conducted an audit of the LG&E Energy Corp. (LEC) and its Subsidiaries' e-Procurement system. The objectives of this engagement were to:

- perform a post implementation review;
- verify that implementation met time, quality, and budget estimates; and
- verify that implementation achieved the functional business objective defined in the business case.

1.1.2 The scope of the audit included a review of policies and procedures related to the system, review of the development process, data security, and other items identified during the audit.

1.1.3 Audit procedures included reviewing documentation of procedures and interviewing members of the Information Technology (IT) and the Supply Chain Departments.

1.1.4 Personnel contacted during the audit were very cooperative.

1.2 Conclusion

1.2.1 Audit Services has determined that the e-Procurement system has adequate and effective internal controls. The e-Procurement system was delivered according to schedule, and with all expected functionality to submit and track purchase requests electronically. Clients are satisfied with the functionality of the system.

1.2.2 As described in the following paragraphs the benefits anticipated from this project have not been realized.

1.2.3 The e-Procurement project was not completed within the original budget estimates. Appropriate approval was obtained for an additional investment of $250,000. However, Supply Chain transferred $248,682 from other projects for additional funding without benefit of an approved Authorization for Investment Proposal. In total the completed project cost of $1,825,000 was 28 percent over the original budget.

1.2.4 Higher than expected costs of joining the internet exchanges, necessary to efficiently bring buyers and sellers together, were not included in the business case. LEC has, to date, opted not to join these exchanges because the cost could not be justified and the savings could not be realized.

1.2.5 The internet exchange markets have not developed as predicted by two well known consulting groups relied upon for the original business case.

1.3 Main Findings and Recommendations

1.3.1 One cause for the less than successful outcome of the project was the weaknesses inherent in the Business Case process. Since that time the Company has taken steps to strengthen the process for project approval. In particular, a detailed risk analysis, including risk identification and assessment of the likelihood and impact of the risk, is now required.

1.3.2 In light of the reduced potential for future benefits from this project, Supply Chain management should work with Accounting personnel to determine the appropriate carrying value of this software on the LEC balance sheet.

1.3.3 The e-Procurement project was initiated according to the Company Capital Policy, by submitting a Business Case. Company policies are posted and maintained on the Company Intranet site allowing employees to access the most current information as needed. However, the policies and procedures have changed and the current Capital policy posted on the Intranet does not contain the new guidelines pertaining to the Authorization for Investment Proposal process.

2 IMPLEMENTATION PLAN USAS IS-02-E-155

Implementation Meeting: Conducted through e-mail **Present:** Management: D. Holden, V. Scott, G. Watkins

Date: Various Audit Services: Lisa Buckner

Issues	Agreed / Not Agreed	Management Action Plan	Person Responsible	Date to be Completed	Management's Follow-up Comments / Date
4.1.9 Review the e-Procurement system to determine if the asset is properly valued.	Agreed	Supply Chain management will address the valuation of the system with Property Accounting and others as necessary.	G. S. Watkins	05/30/03	
4.1.13 Update the existing Company policies and procedures located on the Intranet to reflect the new Authorization for Investment Proposal (AIP) process.	Agreed	The AIP form and the Capital Evaluation Model were updated and posted to the Intranet site in February 2003. The underlying policy will be updated to reflect organizational and administrative changes that have been made since the policy was issued in July 2000.	V. L. Scott	05/30/03	
4.1.15 IT support personnel use a generic logon ID for accessing production data.	Agreed	IT Service Delivery will request unique logon IDs and passwords for each support person.	D. L. Holden	12/31/02	Implemented

3 BACKGROUND

3.1.1 In 2000, e-Procurement was identified as a strategic initiative and an important milestone for placing the organization in a position to do business via the internet. The long-term vision was to create a low-cost procurement process that relies on third party exchanges to provide the system and database maintenance.

3.1.2 Functionally, the e-Procurement system provides the necessary features to submit and track purchase requests electronically. However, several assumptions as to the throughput into the system and the resulting savings did not come to fruition.

3.1.3 The e-Procurement project business case was approved based on information obtained from two well-known industry consulting organizations, Gartner and Meta groups. In 2000, these groups estimated that 2.1 trillion dollars worth of goods and services, approximately 9.4 percent of the total U.S. economy, would be purchased via the internet by 2003. From these predictions a host of assumptions were made by leaders of the industry as to the potential benefits to be reaped through participation in e-Procurement ventures. In many instances these assumptions did not come to pass.

3.1.4 The basis of estimated internet spending was derived from the anticipated formation of buying exchanges, bringing both buyers and sellers together efficiently and for less cost than traditional paper-based or Electronic Data Interchange (EDI) processes. At that time, it was predicted that suppliers would join these exchanges and offer substantial discounts to the exchange members.

4 DETAILED FINDINGS AND RECOMMENDATIONS

4.1.1 The buying exchanges have run into limitations and were not formed as rapidly as anticipated. Furthermore, the cost of joining these exchanges was underestimated and not included in the business case as a cost of the project. In the current environment, any potential savings could only be obtained from joining an exchange; however, due to the cost of joining such an exchange and the uncertainty of the ability to realize real savings, LG&E Energy Corp. (LEC) has opted not to join at this time.

4.1.2 Savings were to be achieved by leveraging LEC's aggregated spending with other utilities through an exchange. These exchanges were formed during the inception of this project and now exist in the form of Pantellos and Enporion. At the time, it was predicted that the aggregated spending would entice suppliers to participate in the exchanges and offer discounts to the exchange members. However, suppliers were reluctant to join the exchanges. Suppliers had little or no incentive to participate or to lower their per-unit cost to attract new customers. In some exchanges, suppliers were initially required to pay a fee to participate in the exchange, thus incurring additional expense to service existing customers with no commensurate benefit.

4.1.3 The original Authorization for Capital Expenditure for the e-Procurement project requested $1,311,929. However, this amount was not sufficient to complete the project. To cover the costs, the Supply Chain Department submitted an Authorization for Investment Proposal in the amount of $250,000 and transferred $248,000 from other projects. The Director of Supply Chain at the time of the policy breach, is no longer with the Company. Current management is aware of the revised policy.

4.1.4 The project was completed at a total cost of $1,825,000, 28 percent over budget.

4.1.5 In the business case, estimated first-year spending through e-Procurement was $22 million. In actuality, about 10 percent of that spending was realized due to reasons explained above. LEC savings were estimated at $725,000 for year one and $1.4 million for year two, little of which is anticipated to be realized.

4.1.6 **Recommendation:** In light of the fact that only a fraction of the anticipated savings will be achieved, Audit Services recommends that Supply Chain Management continue its review and evaluation of the contribution this project is making to the achievement of its business objectives. Supply Chain Management should work with Accounting personnel to determine the appropriate carrying value, if any, of this software on the LEC balance sheet.

4.1.7 With the implementation of e-Procurement it was anticipated that LEC would be able to decommission the existing order system (WebReq). However, due to time and cost limitations, the decision was made to use the existing interface to Oracle rather than create a new interface. In an effort to realize savings, vendor support for WebReq was discontinued as of May 2001. Additionally, vendor support for e-Procurement will be discontinued at year end. In the event support is required for e-Procurement, support can be purchased on an as needed basis. Though WebReq is no longer vendor supported, IT has several staff on hand that are familiar with the system and capable of providing maintenance/support.

4.1.8 In Spring 2000, LG&E met with several technology providers of e-Procurement solutions to review their product offering. At that time, Commerce One was considered the e-Procurement exchange technology engine for the utility industry. Due to Commerce One's strong position in the e-Procurement market at that time, LG&E chose Commerce One as their e-Procurement provider. In March 2000 Commerce One boasted a stock-market value of $21 billion and shares sold at the split-adjusted equivalent of $1,356. In October 2002, Commerce One shares could be bought for just over $3, and its stock-market value had shrunk to less than $100 million. In light of Commerce One's current financial position, continued business viability is questionable.

4.1.9 Audit Services concurs with the organization's actions to strengthen the justification for project implementation. In many instances the areas of weakness detected in the format and requirements for submission of the business case used for the e-Procurement project have been minimized by the format and requirements for submission of the Investment Proposals used today. In particular, a detailed risk analysis including risks and both the likelihood and the impact of the risk is vital for consideration in addressing prudent business decisions. Currently, the Company Intranet site Peoplelink contains information related to submission of a business case rather than the process for submitting an Investment Proposal.

4.1.10 **Recommendation:** The new format and requirements for the submission of an Investment Proposal should be posted on the Company Intranet site. Providing employees with the most current information and expectations in a centralized and convenient location will be beneficial in the enforcement of Company policy and procedure.

4.1.11 From a technological perspective, e-Procurement was found to function as intended. Information Technology controls, in general, were found to be secure and sufficient. In addition, clients are satisfied with system performance. Audit Services noted, however, that Information

Technology support personnel use a generic logon ID for accessing and maintaining production data. The use of a generic logon ID does not provide an appropriate audit trail.

4.1.12 **Recommendation:** Audit Services recommends that each support person log in with a unique ID and password. This will provide an audit trail and accountability of any changes made to production data.

APPENDIX I

ENGAGEMENT MEMO

From: Balderson, Carl
To: Wendy Welsh
Cc: V.A. Staffieri, Richard Aitken-Davies, Richard Barham, Diane Holden, Kathy Butler, Mike Miller, Joe Hayes, Gary Watkins
Subject: LEC & Subsidiaries – E-Procurement
Date: September 11, 2002

Audit Services has scheduled an audit of LG&E Energy Corp. and subsidiaries' E-Procurement application, with preliminary survey work beginning the week of September 16, 2002. The objectives of this engagement are to perform a post-implementation review to determine that application data control procedures and operations are adequate and effective; and to verify that implementation of the system met time, quality, and budget estimates.

The scope of the audit will include a review of policies and procedures related to the system, review of the system development process, data security, and other items identified during the course of the audit. We will encourage the involvement of your staff in identifying process improvements.

The audit will be performed by Lisa Buckner, Information Systems Auditor under the direction of Debbie Shelton, Manager of Information Technology and Operational Auditing. We look forward to working with you and your staff during this engagement. Please advise Debbie Shelton if you would like to schedule an opening conference to provide you an opportunity to discuss the audit objectives, scope, and timing; or you may call me with any questions or comments.

Carl

Audit Services

Audit Report No. IT08U835

E.ON U.S. Services Inc.

PowerPlant/PowerTax Post-Implementation Review

Date Issued: January 29, 2009

E.ON U.S. LLC Audit Services
PowerPlant/PowerTax Post-Implementation Audit
IT08U835

Reviewed Departments:	Information Technology Service Delivery, Property Accounting, Corporate Tax
Subject of Audit:	PowerPlant/PowerTax Post-Implementation Audit
Auditor(s):	L. H. Buckner
Reviewers:	P. F. Tirey, D. A. Shelton
Fieldwork Completed:	December 26, 2008
Draft Report Issued:	December 29, 2008
Final Report Issued:	January 29, 2009

To:

Senior Vice President, Information Technology	W. C. Welsh
Chief Financial Officer	S. B. Rives
cc:	
Chief Executive Officer	V. A. Staffieri
Vice President Decentralized Audit Department (E.ON AG)	Dr. T. Fecker
Director, Information Technology Service Delivery	K. A. Butler
Director, Utility Accounting and Reporting	S. L. Charnas
Manager, Information Technology Service Delivery	A. R. Hall
Director, Corporate Tax	R. L. Miller
Manager, Information Technology Service Delivery	A. Moore
Controller	V. L. Scott
Manager, Tax Accounting	J. S. Williams
Manager, Property Accounting	S. L. Wiseman
PricewaterhouseCoopers (PwC)	L. A. Prather
PricewaterhouseCoopers (PwC)	J. M. Zoglmann

1 Management Summary

1.1 Introduction

1.1.1 Audit Services completed a post-implementation review of the PowerPlant/PowerTax project. The scope of the audit included a review of associated documentation and interviews with personnel from Information Technology Service Delivery (ITSD), Property Accounting, and Tax Accounting.

1.1.2 The objectives of this review were to determine that

- the application data control procedures and operations are adequate and effective;
- the system is efficiently meeting user requirements; and
- the implementation met time and budget estimates.

1.2 Conclusion

1.2.1 Audit Services concludes that the project was implemented on time and within budget, data control procedures and operations are adequate and effective, and the application is meeting user requirements. During detailed testing it was noted that the Project Charter was completed but not signed. Additionally, client sign-off for key points in the project plan was obtained, but not documented and retained. Both of these evidentiary requirements are considered significant controls.

1.2.2 Internal Control System (ICS) relevant findings do exist which should be considered within the scope of the group-wide evaluation and aggregation of deficiencies. These issues, missing signatures on the Project Charter and documentation of the client sign-off points, do not represent significant risks to the financial reporting system. As of December 31, 2008, both action items were implemented and remediated.

1.3 Main Findings and Recommendations

1.3.1 Based on procedures performed, improvements are needed in the area of document retention.

1.3.2 The non-ICS related audit issue is listed in the table in Appendix 1, and the ICS related issues are listed in Appendix 2.

2 Background

2.1 Overview

2.1.1 The Oracle Financial Materials System (OFMS) Fixed Assets module did not provide adequate functionality for Property Accounting functions and as a result, critical Property Accounting functions were handled in spreadsheets outside of OFMS. Additionally, many critical Tax Accounting functions were also handled in spreadsheets due to the limitations of the Acufile system. To resolve these issues a search was conducted for a new fixed asset/tax software solution and the PowerPlant/PowerTax modules were selected for implementation. The modules were fully implemented by June's 2008 close. The modules track capital expenditures, manage book and tax depreciation, calculate the tax provision, and address various regulatory requirements. The implementation also eliminated multiple manual processes and the Acufile application for managing fixed assets and calculating tax provision.

2.1.2 Since the PowerPlant/PowerTax System is used to generate journal entries and tax adjustments that directly impact the financial statements, the system is in-scope for the purposes of Internal Controls.

3 Detailed Report

3.1 Auditing Procedures Performed

3.1.1 Audit Services reviewed project documentation and met with various clients from Information Technology (IT), Property Accounting, and Tax Accounting.

3.2 Findings and Recommendations

3.2.1 One of the key systems development ICS controls require the definition of project sign-off points (client approvals) during the project life cycle. The PowerPlant/PowerTax project plan included the provision of sign-off points. Through interviews and review of documents associated with the project, it was determined that the client had agreed with the progress of the project. However, documentation (sign-offs) supporting the approval was not maintained. The procedures for sign-offs during the project life cycle do not address the retention of documentation to support the approval.

3.2.2 **Recommendation:** ITSD should meet with the client and document client approval of major sign-off points for historical purposes.

3.2.3 **Recommendation:** ITSD should consider reviewing the current procedures for sign-off points on major projects.

3.2.4 IT procedures and internal control C.09.05.00.02 requires that the key stakeholders and team members sign-off on the Project Charter. However, the Project Charter for the PowerPlant**/**PowerTax project did not have documented signatures.

3.2.5 **Recommendation:** ITSD should review with the appropriate IT personnel the need to ensure the Project Charter includes all required signatures.

3.2.6 Interviews were conducted with Property Accounting and Corporate Tax employees to determine that the project met user requirements. No exceptions were noted.

3.2.7 Audit Services reviewed project documentation and conducted interviews to determine that the project budget and timing requirements were met. No exceptions were noted.

3.2.8 Testing for appropriate user access, approval of users with access, removal of terminated or transferred employees, change management, and data backup procedures was performed during ICS interim and update testing. No exceptions were noted.

3.2.9 The interfaces for PowerPlant/PowerTax were tested by obtaining a list of the interfaces and selecting one manual and one automatic interface and ensuring processes were in place to address any errors if the interface did not run successfully. No exceptions were noted.

3.2.10 The issues regarding the signatures on the Project Charter and the documentation of the client sign-off points do not represent significant risks to the financial reporting system. As of December 31, 2008, both action items were implemented and remediated.

Ref.	Recommendations	Management Action Plans	Person Responsible	Date to be Completed	Follow-Up
3.2.3	ITSD should consider reviewing and standardizing the current procedures for sign-off points on major projects.	ITSD will revise and standardize the procedures for documenting client sign-off points.	A. R. Hall	3/31/2009	

E.ON U.S. LLC Audit Services
PowerPlant/PowerTax Post-Implementation Audit
IT08U835

Allocation of ICS relevant findings to process, control objectives and risk according to the central process catalog.

Number	Finding	Process	Control Objective	Risk	Recommendation	Management Action Plans	Person Resp.	Date Completed
3.2.2	One of the key systems development ICS controls requires the definition of project sign-off points (client approvals) during the project life cycle. The PowerPlant/PowerTax project plan included the provision of sign-off points. Through interviews and review of other documents associated with the project, it was determined that the client had agreed with the progress of the project. However, documentation supporting the sign-offs was not maintained.	C.09.05.00.02	Adequate implementation and maintenance	Inadequate documentation	ITSD should meet with the client and document client approval of major sign-off points for historical purposes.	ITSD will document the client agreement with the major sign-off points that were included in the original project plan.	A. Moore, A. R. Hall	This action item was implemented December 29, 2008.
3.2.5	IT procedures and internal control C.09.05.00.02 requires that the key stakeholders and team members sign-off on the Project Charter. However, the Project Charter for the PowerPlant/PowerTax project did not have documented signatures.	C.09.05.00.02	Adequate implementation and maintenance	Inadequate documentation	ITSD should review with the appropriate IT personnel the need to ensure the Project Charter includes all required signatures.	ITSD will communicate to the appropriate personnel the requirement of acquiring all signatures for a Project Charter.	A. Moore	This action item was implemented December 19, 2008.

Audit Services

LG&E Energy LLC

Entities Included:

- **Kentucky Utilities Company,**
- **LG&E Capital Corp.,**
- **LG&E Energy LLC,**
- **LG&E Energy Marketing,**
- **LG&E Energy Services,**
- **Louisville Gas and Electric Company, and**
- **Western Kentucky Energy Corp.**

Audit: **Sarbanes-Oxley Act (SOA) Section 404**

Testing of the design and operating effectiveness of internal control over financial reporting.

Tested Entities :	• Kentucky Utilities Company (KU), • LG&E Capital Corp. (LCC), • LG&E Energy LLC (LEL), • LG&E Energy Marketing (LEM), • LG&E Energy Services (SERVCO), • Louisville Gas and Electric Company (LG&E), and • Western Kentucky Energy Corp. (WKE)
Auditing Division:	LG&E Energy LLC Audit Services
Audit Subject:	Testing of the design and operating effectiveness of internal controls over financial reporting
Audit Location(s):	LG&E Energy LLC
Auditors:	LEL Audit Services under the direction of Mrs. Shelton, Director, Audit Services
Date of Audit Report:	February 15, 2005

List of Recipients:

Senior Vice President, Audit, E.ON AG	Dr. Holtmann
Vice President IT and Project Audit	Mr. Joachim
Chief Executive Officer	Mr. Staffieri
Chief Financial Officer LEL	Mr. Rives
Executive Vice President, General Counsel & Corporate Secretary	Mr. McCall
Senior Vice President - Energy Delivery	Mr. Hermann
Senior Vice President - Energy Services	Mr. Thompson
Director Supply Chain LEL	Mr. Watkins
PwC – Louisville	Mr. Moore

Index

1 Management Summary

1.1 Overall Result

The audit exposed no material weaknesses in internal controls over financial reporting. Several deficiencies were identified, the majority of which were related to retention of evidence of control. Some instances of significant deficiencies were acknowledged and are currently being addressed. Findings were evaluated per the guidance provided from the E.ON AG Central Project Team.

1.2 Overview of Audit Topic Results

The following chart shows an overview of the result of each audit topic.

	Appendix 1 Reference Numbers	Audit Topics	Inconsequential or no Deficiencies	Deficiencies	Significant Deficiencies
3.1		**Summary of Significant Deficiencies**			
3.1.1	1	Entity Scoping			
3.1.2	2-4	Process Scoping			
3.1.3	17	Coverage of Significant Accounts and FSA			
3.2		**Management Controls**			
3.2.1	5-8	Control Environment			
3.2.2	9-10	Information and Communication			
3.2.3	11-21	Monitoring Controls			
3.3		**Process Level**			
3.4		**Control Activity Level**			
3.4.1	22-23	B.01 Risk Assessment			
3.4.2	24-29	C.01 Revenue and Receivables			
3.4.3	30-37	C.02 Purchasing and Payables			
3.4.4	38-41	C.03 Payroll and Employee Benefits			
3.4.5	42-47	C.04 Fixed Assets			
3.4.6	48-53	C.05 Inventory			
3.4.7	54-55	C.06 Production/Operations			
3.4.8	56-60	C.07 Treasury/Cash and Trading			
3.4.9	61-66	C.08 Ledger Maintenance, Closing, Financial Reporting			
3.4.10	67-80	C.09 Information Technology			
3.4.11	81	C.10 Tax			
3.4.12	82-87	C.11 Legal			
3.4.13	Not Applicable	C.12 Corporate Strategy and Development			

1.3 Major Findings and Recommendations

The audit exposed no material weaknesses in internal controls over financial reporting. Significant deficiencies resulted in specific recommendations regarding scoping; management monitoring controls; and control activities in the Information Technology and the Ledger Maintenance, Closing, and Financial Reporting cycles which are documented in section 3.1. Additional recommendations were communicated to management, as discussed in section 3.4, addressing one of four categories of issues regarding documentation, SAP MIC, evidence, or control issues. Recommendations are detailed in Appendix 1. Management developed appropriate action plans, and assigned a suitable due date and ownership responsibility for each recommendation. These action plans are monitored by Audit Services as part of the monthly issues tracking and quarterly reporting process to ensure appropriate and timely resolution.
This report was discussed with the Sarbanes-Oxley Steering Committee and was submitted to the LEL Audit Committee.

February 15, 2005.

Mrs. Logan	Mrs. Shelton
Project Manager Sarbanes-Oxley	Director of Audit Services LEL

2 Audit Scope

As mandated, LEL Audit Services systematically tested the design and operating effectiveness of the SAP Management Internal Controls (MIC) documented and implemented internal controls over financial reporting. The procedures used in 2004 do not constitute an audit of internal controls conducted in accordance with the standards of the Public Company Accounting Oversight Board (PCAOB) such as will be performed by PricewaterhouseCoopers LLP - Louisville (PwC) and LEL Audit Service (Audit Services) in subsequent years. The completion of these additional procedures in subsequent reviews might reveal other matters that will be reported at that time.

The testing was carried out between September 1, 2004 and January 30, 2005.

The testing focused on

- the entity and process scoping,
- the coverage of significant accounts,
- the process documentation,
- the process design,
- the control documentation,
- the control design, as well as
- the implementation of control activities and the evidence of the correct execution of controls.

Financial statement assertions were not available at the time of review. Therefore, these assertions were excluded from Audit Services' focus of test work and are reported as a significant deficiency.

Inquiry, observation, examination, and reperformance were used at various stages as testing methods. The basis for the testing was the central guidelines developed by E.ON Corporate Audit and the testing concept of E.ON Audit Services GmbH (E.ON AS) dated August 18, 2004. The test sample was selected according to the related risks as defined through LEL Audit Services' evaluation.

PwC Louisville reviewed the Company's entity scoping documentation based on amounts included in the September 30, 2004 FRANGO submission. The review was conducted in accordance with the guidance provided by the E.ON AG Central Project Team. PwC Louisville provided a number of specific comments and recommendations for improving documentation of the mapping of significant processes to specific financial statement line items, project scoping by or-

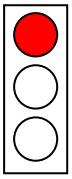
ganization unit, calculation of financial statement line item coverage percentages, and consideration of the following specifically-requested subjects (independent of any quantitative criteria) - Risk Assessment, Ledger Maintenance and Closing, Information Technology, and Management Controls. All audit topics were tested jointly by LEL Audit Services and PwC Louisville.

The appropriate implementation of the recommended measures on deficiencies and significant deficiencies will be tested as part of the testing conducted in 2005.

3 Detailed Report

3.1 Summary of Significant Deficiencies

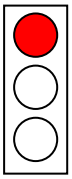
Process Scoping (3.1.2)



General Assessment: Significant Deficiency

Appendix 1 Reference Numbers .	Recommendation	Responsible	Deadline
2	Identify LEL Significant Accounts and map accounts to processes and sub-processes for the 2005 Sarbanes-Oxley Section 404 Compliance Project.	G. Watkins	March 31, 2005
3	Document the process supporting goodwill.	V. Scott	June 30, 2005
4	Document the process detailing regulatory assets and liabilities.	V. Scott	June 30, 2005

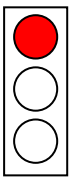
Coverage of Significant Accounts and Financial Statement Assertions (3.1.3)



General Assessment: Significant Deficiency

Appendix 1 Reference Numbers .	Recommendation	Responsible	Deadline
17	Timely completion of Financial Statement Assertions should be completed.	G. Watkins	March 31, 2005

Management Controls - Monitoring (3.2.3)



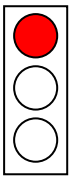
General Assessment: Significant Deficiency

Several recommendations for increased levels of documentation and retention of evidence were made as a result of the Management Control Survey. Significant deficiencies were noted in the monitoring cycles as it addressed the areas of the SOA project noted as significant deficiencies above, primarily the identification of significant accounts and completion of financial statement assertions.

Appendix 1 Reference Numbers .	Recommendation	Responsible	Deadline
15	Management should ensure that compensating internal controls are in place to mitigate control limitations inherent in the current design of the reporting and management structure (i.e., lack of independence in board personnel and Audit Services reporting structure). The compensating internal controls around these processes should be identified, documented, and monitored for effectiveness.	B. Rives	March 31, 2005
17	Timely completion of Financial Statement Assertions should be completed.	G. Watkins	March 31, 2005
19	Management should develop a process for cycle leads and process owners to report internal control deficiencies in a consistent manner. Internal controls around this process should be identified, documented, communicated, and monitored for effectiveness.	G. Watkins	March 31, 2005

Appendix 1 Reference Numbers .	Recommendation	Responsible	Deadline
21	A process for identifying and addressing changes in United States Generally Accepted Accounting Principles (US GAAP) is needed. Internal controls around this process should be identified, documented, communicated, and monitored for effectiveness.	B. Rives	March 31, 2005

Control Activity Level - C.08 Ledger Maintenance, Closing, Financial Reporting (3.4.9)

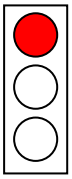


General Assessment: Significant Deficiency

Documentation gaps, in addition to the specific recommendations listed below, were contributing factors for a rating of Significant Deficiency.

Appendix 1 Reference Numbers	Recommendation	Responsible	Deadline
62	Balance sheet reconciliations are performed subsequent to the close of the books; thus, errors found can only be corrected in the subsequent period or topside, depending on the timing. Other key controls should be identified that give assurance that amounts reported in the financial statements are complete, accurate, and valid.	V. Scott V. Strange S. Williams	March 31, 2005
63	The process for determining, evaluating, and communicating materiality judgments should be documented and communicated.	L. Dalton	October 31, 2005
64	Procedures for journal entries and account reconciliations are not formally documented. When finalized, documented procedures should be communicated to personnel and evidence of communication should be maintained.	V. Scott V. Strange S. Williams	January 31, 2005

Control Activity Level - C.09 Information Technology (3.4.10)



General Assessment: Significant Deficiency

Documentation gaps, in addition to the specific recommendations listed below, were contributing factors for a rating of Significant Deficiency.

Appendix 1 Reference Numbers	Recommendation	Responsible	Deadline
67	LEL should implement regular testing of backup tapes. Tests should be performed at a minimum on a quarterly basis. All tests should be documented for future reference.	M. Spurlock P. Mukundan	March 31, 2005
74	Management should communicate and enforce the current emergency change policy. Management should ensure that a Request for Change (RFC) is created for all emergency changes prior to or immediately after migration.	M. Spurlock T. Hall	March 31, 2005
75	Management should enforce current change management policy and ensure that all changes are appropriately requested, approved, and tested prior to being moved into the production environment.	M. Spurlock T. Hall	March 31, 2005
77	LEL should enforce the new user administration process to ensure that all new access requests appropriately submitted and approved and that documentation is maintained.	M. Spurlock K. Fowler	March 31, 2005

3.2 Management Controls

Audit Services and PwC completed a high-level review of the Management Controls cycles including Control Environment, Information and Communication, and Monitoring of Controls to assess the tone at the top and the adequacy of LEL's control environment. Procedures were based upon guidance and general topics in the E.ON management control survey and included a limited number of interviews. Testing of operating effectiveness was limited primarily to inquiry.

Based on the limited procedures performed, it appears that LEL has an adequate control environment to demonstrate an effective tone at the top. However, areas exist where a basis for an opinion could not be derived. Recommendations for improvement are included in Appendix 1. These recommendations address ensuring appropriately documented and clearly defined internal controls of significant processes, as well as enhancing awareness of some controls that are currently in place but not widely understood.

Generally, in the coming year management should clearly identify, document, and monitor internal controls over each facet of the control environment, information and communication, and monitoring functions. In all cases, evidence of the operation of significant controls should be maintained and available for oversight and review.

It should be noted that procedures did not constitute an audit of internal controls conducted in accordance with the standards of the PCAOB such as will be performed by both PwC and Audit Services in subsequent years. The completion of these additional procedures in subsequent years might reveal other matters that will be reported at that time. A much more in-depth review, including substantive testing, will be performed in 2005.

3.3 Process Level

Process level testing focused on management's design of each cycle, identifying the inclusion and exclusion of the appropriate processes. Additionally, walkthroughs were performed to ensure documented procedures matched management performed controls.

Prior to testing a risk assessment was performed across all processes. Testing was performed on those processes deemed as highest risk. In addition, Audit Services and PwC ensured that a walkthrough was conducted for at least one process in each cycle. Walkthrough results consistently included the following general findings for the majority of the documentation: management placed too much reliance on the Committee of Sponsoring Organizations (COSO) Framework / E.ON generic model, differences between the documented process and the actual process exist, significant controls were not always identified, activities that are part of the process were, at times, inappropriately identified as controls, links to and from other processes were largely absent, some processes were not documented, and several inconsistencies were found within the documentation.

To address these issues LEL Management performed the following actions in regard to the SOA project: a full-time Project Manager in addition to Director level oversight was assigned; a Steering Committee, consisting of Senior Management, was instituted; more comprehensive documentation guidelines were created and distributed; documentation was rewritten by cycle leads based upon the new guidelines and specific recommendations provided by Audit Services and PwC; meetings of the Steering Committee are held weekly, as are meetings between the Project Manager and the cycle leads, to address issues, concerns, and approaching deadlines; the Project Manager, PwC, and Audit Services, meet weekly to communicate and address issues, concerns, and approaching deadlines; and Ernst & Young LLP (E&Y) is currently performing a high level assessment of the 404 Project to be completed by mid-February 2005. Revised documentation has not yet been reviewed but will serve as the base for testwork in 2005. Management has created a project plan to include remediation of all deficiencies identified from the 2004 exercise in the first and second quarter of 2005.

3.4 Control Activity Level

Audit Services and PwC tested 1,340 control activities for an overall coverage of 31 percent of the control activities included in the SAP MIC tool as of September 30, 2004. Testing was conducted across all cycles jointly by Audit Services and PwC. Procedures were developed and conducted to ensure appropriate coverage was obtained for this test year[1] and do not constitute an audit of internal controls conducted in accordance with the standards of the PCAOB such as will be performed by PwC and Audit Services in subsequent years. The completion of these additional procedures in subsequent reviews might reveal other matters that will be reported at that time. Various levels and testing techniques were utilized in the testing process including inquiry, observation, examination, and reperformance.

Following testing, a memo detailing results was generated for each cycle and shared with management. Management developed appropriate action plans and assigned a suitable due date and ownership responsibility for each recommendation. Recommendations typically address one of four categories of issues regarding documentation, SAP MIC, evidence, or control issues. The following general recommendations apply to all cycles across the market unit level:

- Documentation recommendations focus on controls that are present but not documented, process steps erroneously identified as controls, and processes that were omitted from documentation exercises.
- SAP MIC recommendations focus on amending the data in the SAP MIC tool, ensuring control characteristics (e.g., Completeness/Accuracy/Validity/Restricted Access [CAVR], Automated/Manual, Preventive/Detective, etc.) are consistent across all entities where appropriate, and matching the data in the SAP MIC tool to the documentation for consistency.
- Evidence recommendations vary as to significance, however the focus was on ensuring appropriate documentation evidence is maintained for controls that are functioning. This might include signatures or initials on reviews, maintaining checklist, or requesting confirmations.
- Control recommendations identify opportunities for management to strengthen specific internal control design and internal control operating effectiveness.
- Entity-level recommendations focus on the need for LEL Management to identify and document key spreadsheets and non-standard reports, such as those generated from the Oracle Financial Management System. A process is to be developed and utilized as part of the individual cycles to ensure that appropriate re-

[1] **Test Year** – E.ON and the LEL market unit were excluded from 404 compliance for the year-ended December 31, 2004.

stricted access, change control, and other Information Technology-related controls exist and that accurate and complete information is processed and reported. In addition, a process is needed to identify service organizations that are significant to the Company's internal control over financial reporting. An assessment process should then be developed and documented to determine if a SAS 70 report exists and is sufficient in scope.

Evidence and control recommendations are specific and are listed individually in Appendix 1, LEL SOA Recommendations.

Appendix I
LG&E Energy LLC – Audit Services
LEL SOA Recommendations
February 15, 2005

	Cycle	Entity	Recommendation	Responsible	Deadline
1	Entity Scoping	LEL	Assemble the necessary documentation to evidence appropriate entity level scoping for the 2005 Sarbanes-Oxley Section 404 Compliance Project.	G. Watkins	March 31, 2005
2	Process Scoping	LEL	Identify LEL Significant Accounts and map accounts to processes and sub-processes for the 2005 Sarbanes-Oxley Section 404 Compliance Project.	G. Watkins	March 31, 2005
3	Process Scoping	LEL	Document the process supporting goodwill.	V. Scott	June 30, 2005
4	Process Scoping	LEL	Document the process detailing regulatory assets and liabilities.	V. Scott	June 30, 2005
5	Management Level Survey	LEL	The roles and responsibilities of the Compliance Officer should be clearly defined and documented with at least an annual review.	J. McCall	March 31, 2005
6	Management Level Survey	LEL	Internal controls should be identified, documented, communicated and monitored for effectiveness for the whistleblower and employee hotlines. Procedures should include formal logging and tracking of calls received on the hotline and emails received. Dissemination of the calls for follow-up and tracking of results should be documented, as well.	P. Pottinger	March 31, 2005
7	Management Level Survey	LEL	Management should review the function of each hotline and determine if perhaps one hotline for all calls would be more beneficial for employees.	P. Pottinger	March 31, 2005
8	Management Level Survey	LEL	Management should complete its review of the Authority Limit Matrices (ALM) and publish the modifications including documentation of people's assigned roles as to internal controls. Any automation of the ALM in systems such as the Oracle Financial Management System should be expressly documented and test results should be maintained as evidence of control effectiveness.	B. Rives	March 31, 2005
9	Management Level Survey	LEL	Management should provide general awareness of internal controls, their roles, and the importance of the internal controls to employees throughout the organization.	G. Watkins	March 31, 2005
10	Management Level Survey	LEL	Data access control documentation should be updated and should include requirements for routine review of data access by the data owner. Evidence of these reviews should be maintained to demonstrate control effectiveness.	W. Welsh	March 31, 2005
11	Management Level Survey	LEL	'Development of processes, such as FRANGO reporting and risk identification and valuation, should be formalized including documentation and evidence of monitoring of these processes (e.g., supporting documentation for quarterly financial and monthly management reporting). Internal controls should be identified, documented, communicated, and monitored for effectiveness.	B. Rives	March 31, 2005
12	Management Level Survey	LEL	Formal documented approvals of the planning and budgeting process are typically not maintained. Internal controls should be identified, documented, communicated, and monitored for effectiveness.	B. Rives	March 31, 2005
13	Management Level Survey	LEL	Formal documentation of the performance reporting and monitoring process has not been completed (e.g., formal documented approvals of the planning and budgeting process is typically not maintained). Internal controls should be identified, documented, communicated, and monitored for effectiveness for the overall	B. Rives	March 31, 2005

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	Cycle	Entity	Recommendation	Responsible	Deadline
			monitoring process.		
14	Management Level Survey	LEL	a) A policy defining responsibility for reviewing new accounting pronouncements is necessary. b) In addition, PricewaterhouseCoopers (PwC) should not be included as a significant control. Internal controls should be identified, documented, communicated, and monitored for effectiveness for the accounting pronouncement review process.	B. Rives	March 31, 2005
15	Management Level Survey	LEL	Management should ensure that compensating internal controls are in place to mitigate control limitations inherent in the current design of the reporting and management structure (i.e., lack of independence in board personnel and Audit Services reporting structure). The compensating internal controls around these processes should be identified, documented, and monitored for effectiveness.	B. Rives	March 31, 2005
16	Management Level Survey	LEL	Management should continually review internal controls, their documentation, and their monitoring processes.	G. Watkins	March 31, 2005
17	Management Level Survey	LEL	Timely completion of Financial Statement Assertions should be completed.	G. Watkins	March 31, 2005
18	Management Level Survey	LEL	Management should strive to ensure that the information in the SAP Management of Internal Controls (MIC) tool is accurate and complete.	G. Watkins	March 31, 2005
19	Management Level Survey	LEL	'Management should develop a process for cycle leads and process owners to report internal control deficiencies in a consistent manner. Internal controls around this process should be identified, documented, communicated, and monitored for effectiveness.	G. Watkins	March 31, 2005
20	Management Level Survey	LEL	A process, similar to that used in preparing the LG&E and KU 10Q/K should be developed for FRANGO and 20-F reporting. The process should include supporting documentation and evidence of appropriate monitoring and approvals.	B. Rives	March 31, 2005
21	Management Level Survey	LEL	A process for identifying and addressing changes in United States Generally Accepted Accounting Principles (US GAAP) is needed. Internal controls around this process should be identified, documented, communicated, and monitored for effectiveness.	B. Rives	March 31, 2005
22	Risk Assessment	LEL	Audit Services recommends storing the electronic drafts and finalized Risk Reports on a shared network drive that is backed up on a periodic basis and is accessible only by the Director Planning and Controlling department.	A. Tillack	January 13, 2005
23	Risk Assessment	LEL	Audit Services recommends creating a checklist for those control activities items that are “checks” by the Director Planning and Controlling to evidence that the review occurs for all risk information provided by the Business Units.	A. Tillack	January 17, 2005
24	Revenue and Receivables	KU LGE	Audit Services recommends that a monthly close procedure of the Customer Information System (CIS) be created. This could reduce data capture, reconciliation, reporting, and manual work around issues.	F. Mazza	Not Agreed
25	Revenue and Receivables	KU	Audit Services recommends the CIS system generate a detailed accounts receivable	F. Mazza	Not Agreed

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	Cycle	Entity	Recommendation	Responsible	Deadline
		LGE	aging report. This report should be utilized during the review of the accounts receivable allowance for doubtful accounts process.		
26	Revenue and Receivables	KU LGE	Audit Services recommends evaluating methods to validate the Unbilled Revenue Model.	F. Mazza	March 31, 2005
27	Revenue and Receivables	KU LGE	Audit Services recommends management review the current method for estimating and recording uncollectible accounts.	F. Mazza	March 31, 2005
28	Revenue and Receivables	KU LGE	Audit Services recommends that an automatic interface between the CIS sub ledger and Oracle Financial Management (OFMS) be utilized to transfer data. This could avoid integrity of data, reporting, reconciliation, and manual work around issues.	F. Mazza	Not Agreed
29	Revenue and Receivables	KU LGE	Audit Services recommends that evidence to support the operating effectiveness of the controls for the billing, sales planning, and contract management process be retained.	F. Mazza	January 31, 2005
30	Purchasing and Payables	KU LGE WKE	During the PwC lead walkthrough of the Demand Analysis (Fuels) documentation, it was noted that (depending on contract terms) title to coal purchased may pass to the Company while in-transit (Free On Board barge) but is not recorded in the accounting records until the coal is unloaded at the generating station. Management should evaluate the need for an accounting accrual for in-transit coal.	E. Thompson-Long	March 31, 2005
31	Purchasing and Payables	KU LGE WKE	During the PwC lead walkthrough of the Demand Analysis (Fuels) documentation, it was noted that no formal policies exist for evaluating potential coal suppliers (bidders) for credit worthiness and likelihood of fulfilling the contract requirements. Management should consider developing procedures to qualify potential coal suppliers.	E. Thompson-Long	March 31, 2005
32	Purchasing and Payables	KU LGE Servco	Two employees with access rights to pay invoices can add/edit the vendor list. Segregation of duties should include responsibilities and information system access rights.	J. Veroff	March 31, 2005
33	Purchasing and Payables	KU LGE Servco	Inventory accrual reconciliations should be documented and retained.	J. Veroff	January 31, 2005
34	Purchasing and Payables	KU LGE Servco	The periodic review of Oracle Financial Management System (OFMS) access by the Manager, Supply Chain Support, should be documented and evidence of the review should be retained.	J. Hayes	January 31, 2005
35	Purchasing and Payables	KU LGE Servco	The Acorde scanning checklist should be completed, retained, and reviewed by a responsible employee as a completeness control.	J. Hayes	January 31, 2005
36	Purchasing and Payables	KU LGE Servco	The periodic review of OFMS access by the Manager, Accounts Payable, should be documented and evidence of the review should be retained.	J. Veroff	December 31, 2004

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	Cycle	Entity	Recommendation	Responsible	Deadline
37	Purchasing and Payables	KU LGE Servco	Stand-alone accounts payable reconciliations should be documented and evidence of the Manager's sign-off should be retained monthly.	J. Veroff	January 31, 2005
38	Payroll and Employee Benefits	LEL	Audit Services recommends the payroll manager approve payroll prior to releasing funds from the Company.	T. Conrad	November 1, 2004
39	Payroll and Employee Benefits	LEL	Audit Services recommends that Payroll identify the exact exception reports used. These exception reports and evidence of the reconciliation / approval need to be retained.	T. Conrad	December 31, 2004
40	Payroll and Employee Benefits	LEL	Management is reviewing checklists used by payroll processors, but there is no evidence of the Payroll Processor who is completing the checklist.	T. Conrad	December 31, 2004
41	Payroll and Employee Benefits	LEL	Audit Services recommends that the documentation for electronic notification from the bank confirming receipt of the deposited pay file be retained.	T. Conrad	December 31, 2004
42	Fixed Assets	KU LGE WKE	Audit Services recommends that controls supporting the selection of depreciation rates are documented and strengthened.	S. Wiseman	March 31, 2005
43	Fixed Assets	KU LGE WKE	Audit Services recommends capital expenditures that exceed the original Authorization for Investment Proposal (AIP) amount by 10% or $100,000 (minimum $25,000) are monitored and reconciled with actual expenditures and revised AIP are issued and reauthorized. Additionally we recommend that the control threshold be reevaluated to ensure that all material variances are properly authorized.	S. Wiseman	March 31, 2005
44	Fixed Assets	KU LGE WKE	Audit Services recommends documenting the System Restoration process that is currently in place.	S. Wiseman	March 31, 2005
45	Fixed Assets	KU LGE WKE	Audit Services recommends that a control is added to ensure positive confirmation is received from all budget coordinators that projects with no activity for 90 days or more should be unitized or remain in Construction Work in Progress (CWIP).	S. Wiseman	March 31, 2005
46	Fixed Assets	KU LGE WKE	Audit Services recommends that evidence to support the operating effectiveness of the controls for the acquiring fixed asset process be retained.	S. Wiseman	March 31, 2005
47	Fixed Assets	KU LGE WKE	Audit Services recommends that review and approvals for the depreciating fixed assets and maintenance process be evidenced through signatures and initials.	S. Wiseman	March 31, 2005
48	Inventory/Fuels	KU LGE WKE	Management should consider whether or not a "blind" receiving count should be adopted, and if not, should consider whether appropriate controls exist around the receiving process (i.e., review of a receiving log or periodic spot checks by the Commercial Manager.	W. L. Bryant	Not Agreed
49	Inventory/Fuels	KU LGE	(Coal) Procedures for reviewing access to the Coal Supply Management System (CSMS) should be established for evidence of review for terminated employees,	E. Thompson-Long	March 31, 2005

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	Cycle	Entity	Recommendation	Responsible	Deadline
		WKE	transferred employees, and role changes related to business functions to ensure that users have appropriate access to CSMS.		
50	Inventory/Fuels	KU LGE WKE	(Gas) Audit Services recommends maintaining evidence of review on Supervisory Control and Data Acquisition (SCADA) system or other department related reports sent to Financial Accounting per dates set in Record Retention policy.	M. C. Satkamp	January 31, 2005
51	Inventory/Fuels	KU LGE WKE	(Coal) Audit Services recommends evidencing review for reconciliations to ensure that inventory disposals/additions are accurately entered into CSMS.	E. Thompson-Long	March 31, 2005
52	Inventory/Fuels	KU LGE WKE	(Coal) Audit Services recommends maintaining evidence of review for the Detail Receipts and Summary of Expenses, the Calculation of Accounts Payable Report, and Monthly Unloading Summary to verify totals agree with supporting documentation.	E. Thompson-Long	March 31, 2005
53	Inventory/Fuels	KU LGE WKE	(Gas) Audit Services recommends retaining evidence of management's review of the annual Internal Inventory Analysis. This evidence should be maintained per requirements set in the Record Retention Policy.	B. R. Walker	March 31, 2005
54	Production/Operations	KU LGE	Personnel that have left the Company should be removed from the Generation Planning restricted access database. The access list should be reviewed at a documented frequency and updated accordingly.	J. P. Malloy	December 31, 2004
55	Production/Operations	KU LGE	Positive confirmation of approvals should be developed and maintained for each facility's unit ratings tests, changes to the forecasting model, and maintenance schedules.	J. P. Malloy	December 31, 2004
56	Treasury/Cash and Trading	KU LEL LGE	PwC noted that the regulated trading back office does not perform a reconciliation of total volumes on a monthly basis similar to the reconciliation performed by the non-regulated back office. Although it was noted that monthly volume reconciliations at a counterparty level are performed, Management should determine if a total reconciliation is needed, as it would incorporate inter-company, and other aspects which the counterparty reconciliations do not address.	N. Smith	September 30, 2005
57	Treasury/Cash and Trading	KU LEL LGE	Treasury should consistently review and sign Electronic Funds Transfer (EFT) forms, for both repetitive and non-repetitive payments, before sending the wire. The EFT forms need to be consistently retained with other documents relating to wires.	D. Lasley	December 31, 2004
58	Treasury/Cash and Trading	KU LEL LGE	The Weekly Forecasts should be reviewed and signed by the Treasurer after preparation.	D. Arbough	December 31, 2004
59	Treasury/Cash and Trading	KU LEL LGE	The Daily Cash Position worksheet should be reviewed and signed by the Team Leader after preparation.	D. Lasley	December 31, 2004
60	Treasury/Cash and Trading	KU LEL	Changes to counterparty credit limits (within the Credit Manager's level of authority) should be documented in the credit files. Documentation should include the effective	J. Early	December 31, 2004

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	Cycle	Entity	Recommendation	Responsible	Deadline
		LGE	date of the change and a short description of the reason for the increase or decrease.		
61	Ledger Maintenance, Closing and Financial Reporting	KU LEL LGE	Audit Services recommends that management consistently review and approve staff prepared non-standard journal entries for the consolidation process prior to posting in a timely manner.	L. Dalton	March 31, 2005
62	Ledger Maintenance, Closing and Financial Reporting	KU LEL LGE WKE	Balance sheet reconciliations are performed subsequent to the close of the books; thus, errors found can only be corrected in the subsequent period or topside, depending on the timing. Audit Services recommends that other key controls be identified that give assurance that amounts reported in the financial statements are complete, accurate, and valid.	V. Strange S. Williams	March 31, 2005
63	Ledger Maintenance, Closing and Financial Reporting	KU LEL LGE WKE	Audit Services recommends that the process for determining, evaluating, and communicating materiality judgments be documented and communicated.	L. Dalton	October 31, 2005
64	Ledger Maintenance, Closing and Financial Reporting	KU LEL LGE WKE	Procedures for journal entries and account reconciliations are not formally documented. This finding was noted in Audit Services "Accounting Controls" report, dated February 2004. Management's action plan stated that the procedures are to be documented by 12/31/04. When finalized, documented procedures should be communicated to personnel and evidence of communication should be maintained.	S. Williams V. Strange	January 31, 2005
65	Ledger Maintenance, Closing and Financial Reporting	KU LEL LGE WKE	Audit Services recommends that financial closing checklists be signed off by the preparer and reviewer and that documentation of the sign off be retained.	V. Strange S. Williams L. Dalton	December 31, 2004
66	Ledger Maintenance, Closing and Financial Reporting	WKE	Audit Services recommends that WKE management retain documentation relating to correcting journal entries or transactions for accounts payable reconciling items.	V. Strange	December 31, 2004
67	Information Technology	KU LEL LGE	LEL should implement regular testing of backup tapes. Tests should be performed at a minimum on a quarterly basis. All tests should be documented for future reference.	P. Mukundan	March 31, 2005
68	Information Technology	LEL	It is recommended that LEL disable accounts after a period of 90 days of inactivity. The account should then be enabled only after contacting the user and verifying that the user is appropriate. User accounts should be reviewed periodically and terminated users accounts should be removed in a timely manner.	K. Fowler	Not Agreed
69	Information Technology	LEL	It is recommended that management review current Unix security settings. Unused and unnecessary accounts should be revoked to strengthen operating system security. Availability of a UNIX shell should be restricted to individuals who require access to perform their daily job function.	K. Fowler	Not Agreed
70	Information Technology	LEL	Audit Services recommends that IT Service Delivery (ITSD) personnel for Trading	J. Ferch	March 31, 2005

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	Cycle	Entity	Recommendation	Responsible	Deadline
			evaluate the issue of users gaining write access without appropriate approval and find an acceptable resolution.		
71	Information Technology	LEL	It is recommended that LEL select the options available to increase the strength of password parameters.	K. Fowler	December 31, 2005
72	Information Technology	LEL	IT Security should consider developing policies and procedures for transferred employees, and role changes related to their business function to ensure users have appropriate access.	K. Fowler	March 31, 2005
73	Information Technology	LEL	It is recommended that LEL review user access lists for terminated employees and remove access in a timely manner.	K. Fowler	December 16, 2004
74	Information Technology	LEL	PwC recommends that management communicate and enforce the current emergency change policy. Management should ensure that a Request for Change (RFC) is created for all emergency changes prior to or immediately after migration.	T. Hall	March 31, 2005
75	Information Technology	LEL	PwC recommends that management enforce current change management policy and ensure that all changes are appropriately requested, approved, and tested prior to being moved into the production environment.	T. Hall	March 31, 2005
76	Information Technology	LEL	PwC recommends that the following Oracle system settings are put in place: 1. The Audit Trail activate profile is enabled especially tables containing critical financial data. 2. Ensure that the Audit Trail Update Tables Report is run and reviewed on a regular basis. 3. Ensure that the Sign-On Notifications profile is set to “YES” for on the Site level. Ensure that Sign-on Password Custom profile is set for Site. Also design a SQL script that will lock a user out after 3 failed login attempts. 4. Set the Sign-on Audit profile to “Form” rather than “User”. Form ensures the highest level of security, also ensure that audit reports detailing failed login attempts are reviewed on a regular basis.	D. Holden	March 31, 2005
77	Information Technology	LEL	PwC recommends that LEL enforce the new user administration process to ensure that all new access requests appropriately submitted and approved and that documentation is maintained.	K. Fowler	March 31, 2005
78	Information Technology	LEL	IT Security should consider documenting security assessment recommendations for all projects on which they consult.	K. Fowler	January 31, 2005
79	Information Technology	LEL	PwC recommends that LG&E communicate their Request for Change (RFC) approval procedures to all staff involved in program changes. Management should perform a periodic review to ensure that changes were approved by an authorized approver.	T. Hall	March 31, 2005
80	Information Technology	LEL	PwC recommends that evidence of user acceptance be documented in writing either via e-mail or a signed document. This documentation should be retained with the RFC in the Magic system for easy identification and review if needed.	T. Hall	March 31, 2005

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	Cycle	Entity	Recommendation	Responsible	Deadline
81	Tax	LEL	Audit Services recommends that reviewers sign off on what they review to provide evidence of the review.	C. M. Garrett	December 31, 2004
82	Legal	LEL	Testing of authority controls indicated that the LG&E Energy LLC Authority Limits Matrix needs to be updated to incorporate the Delegated Powers of Authority Policy, approved on February 10, 2004.	A. Tillack	December 31, 2004
83	Legal	LEL	Testing of restricted access controls over the Corporate Law Department's central file room indicated that the access rights are in need of review to remove employees who have transferred or otherwise no longer require access. Corporate Law Department Management should periodically obtain and review the access to the file room to ensure access is properly restricted.	G. Meiman	December 31, 2004
84	Legal	LEL	Testing of validity controls indicated that the Corporate Law Department does not have a formal process to monitor/evaluate stock transfer agent performance. The Corporate Law Department should consider developing a formal process to monitor and evaluate transfer agent performance. Performance metric should be developed (share reconciliation, number of complaints, etc.) for periodic evaluation.	J. Fendig	February 28, 2005
85	Legal	LEL	During the walk-through, a need was identified to have a responsible employee reconcile the claim information in the Matters Management System (MMS) to claim information reported by Risk Management Services Corp. If possible, this reconciliation should be performed by an employee independent of MMS data input.	G. Meiman	March 31, 2005
86	Legal	LEL	'During the walk-through, a need was identified to formalize the process for communicating and reporting claim information to the Securities Attorney. Controls should be established to ensure the completeness and accuracy of reports provided for disclosure evaluation.	J. Fendig	January 31, 2005
87	Legal	LEL	Audit Services tested the validity controls over easement recording for Louisville Gas & Electric Company (LG&E), Kentucky Utilities Company (KU), and Old Dominion Power Company (ODP). Based on the results of this review the Legal Department should work with KU and ODP to ensure that easements are properly reviewed and signed by an attorney as preparer, as required. This will reduce the potential liability for disadvantageous terms and conditions, and eliminate risks of liability for unauthorized practice of law for the KU agents that are currently signing the documents as preparer.	J. Dimas	January 31, 2005

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Note to Memo – Project Wrap up

To: Central File – 2002 Audit Reports

From: Michelle Mitchell, Corporate Environmental Specialist, Internal Auditor

Re: Kentucky Utilities (KU) Company – Pineville Decommissioning – Memo Report

Audit Services (AS) initiated an environmental evaluation of the decommissioning of the Pineville Generation Station. The objective of this project was to document environmental risk items remaining within the facility boundaries. Environmental Affairs Department staff were present during the initial field visit. An inventory list was drafted and updated as necessary throughout the process of the decommissioning of KU's Pineville Generation Station. AS maintained a continued role throughout the completion of this project.

AS reviewed Company activities that support timely compliance with the accounting rule, Financial Accounting Standards Board (FASB) Statement 143 on *Accounting for Asset Retirement Obligations* that became effective June of 2001 (Standard). The Technical Engineer Supervisor, Lois Sparks is leading this project. There is one task remaining that is planned to be completed by the end of 2003. The Engineering Group is in the planning phase of a Sump Pump Replacement project. This project will replace out-of-service and aged sump pumps in the basement of the main building, with modern, more industrial, less maintenance sump pumps. These pumps will provide a control to flooding in the main generation building basement. TVA Substation equipment will continue to be stored within the building, which requires the avoidance of a wet environment.

The Environmental Affairs Department staff have provided support and regulatory compliance information during the project. The Ash Pond will remain open and monitoring will continue as required. The Sump Pumps will move water from the basement into the pond. This provides a control for the release of possible contaminants into the groundwater or the Cumberland River. Appropriate environmental regulatory agencies have been notified of any changes to the facility's water permit. Facility maintenance and the ash pond water monitoring will be maintained by a part time contractor that has been properly trained by internal personnel to complete all monitoring requirements. There is also a KU – Distribution Operations Station on the frontage of the same property that will remain open.

The Property Accounting Department staff have provided support with the FASB Statement 143 asset accounting retirement obligations notifications to appropriate departments within the company, as well as, outside regulatory agencies. Internal asset monitoring database controls (Oracle) continue to be updated as each task at the facility is completed. This facility was listed in the appropriate internal accounting books as closed at the end of December 2002.

It appears that Company activities support timely compliance with the accounting rule, FASB Statement 143, and no further review is deemed necessary for the remainder of this project. Testing for continued compliance could possibly be included in future Audit Plans.

Cc: C. A. Balderson
D. A. Shelton
TeamMate Workpapers