JIF-04

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

VERIFIED APPLICATION OF LOUISVILLE GAS AND ELECTRIC COMPANY FOR AN ORDER PURSUANT TO KRS 278.300 AND FOR APPROVAL OF LONG-TERM PURCHASE CONTRACT	))))	CASE NO. 2011-00099
VERIFIED APPLICATION OF KENTUCKY UTILITIES COMPANY FOR AN ORDER PURSUANT TO KRS 278.300 AND FOR APPROVAL OF LONG-TERM PURCHASE CONTRACT	))))	CASE NO. 2011-00100

<u>O R D E R</u>

On March 16, 2011, Louisville Gas and Electric Company and Kentucky Utilities Company ("LG&E and KU") filed applications seeking Commission approval of an amended wholesale power contract with the Ohio Valley Electric Corporation ("OVEC") pursuant to the provisions of KRS 278.300.

OVEC was formed in the early 1950s by LG&E and KU and several other utilities and holding companies located in the Ohio Valley region in response to the request of the United States Atomic Energy Commission ("AEC") to supply the electric power needs of the AEC's planned uranium enrichment plant in Pike County, Ohio. OVEC built two coal-fired generating stations and entered into a long-term power agreement with the United States Department of Energy ("DOE"). The agreement gave DOE the right to OVEC's generation capacity. OVEC and its owners or their affiliates, including LG&E and KU, entered into the original Inter-Company Power Agreement ("ICPA"), a 50-year power supply agreement that gave each OVEC owner the right to purchase surplus power not required by DOE in proportion to the owner's participation ratio.

Subsequent to the termination of the DOE power agreement on April 30, 2003, all of OVEC's capacity was considered to be surplus.

The current OVEC ICPA has a term that runs to March 13, 2026.[1] OVEC has recommended extending the ICPA to take advantage of reduced financing costs and to amortize its debt over a longer time period. The resulting savings would be passed on to the OVEC owners through a reduction in energy costs of approximately $1 per MWh from the extension's effective date through the currently scheduled 2026 termination date. It is estimated that LG&E and KU will save approximately $14.3 million on a combined basis over that period of time under the extended ICPA. OVEC and its owners have entered into an amended ICPA, which extends the term an additional 14 years, through June 30, 2040.

LG&E and KU state that, given the relatively low cost of the OVEC generation, they utilize the majority of the power available from OVEC, particularly during peak periods. A comparison of the cost of their own generation and the cost of their OVEC purchases show that the cost per KWh of OVEC's generation compares quite favorably to LG&E's and KU's generation costs.

At the time of the previous extension of the ICPA, OVEC commissioned an independent engineering assessment of the remaining lives and production capabilities, environmental remediation, and decommissioning of its generating facilities. At OVEC's

[1] The current ICPA received Commission approval in Case No. 2004-00395, Application of Kentucky Utilities Company for an Order Pursuant to KRS 278.300 and for Approval of Long-Term Purchase Contract (Ky. PSC Dec. 30, 2004); and Case No. 2004-00396, Application of Louisville Gas and Electric Company for an Order Pursuant to KRS 278.300 and for Approval of Long-Term Purchase Contract (Ky. PSC Dec. 30, 2004).

request, that assessment has been updated since the filing of LG&E's and KU's applications.[2] The results of the updated assessment indicate that, largely due to the generating units having been nearly always operated in a base load mode, with limited thermal cycles of the equipment, the units are expected to be operational at or near their historic operating levels through the term of the ICPA extension, until mid 2040.

The assessment update also indicates that the generating facilities are expected to be in compliance with existing and pending environmental requirements. Selective catalytic reduction devices have been installed on all units over the past decade and flue gas desulfurization equipment will be installed on all units during the 2011-2013 time frame. OVEC does not expect coal combustion by-products to be regulated as a hazardous waste and, therefore, does not anticipate significant future expenditures in this area.

The proposed extension will allow LG&E and KU to continue to receive their shares of OVEC's generation in exchange for payment of OVEC's relatively low costs. As in the past, LG&E and KU will not act as guarantors of OVEC's debts nor will they issue securities or other evidence of indebtedness for the purpose of financing their participation in the Amended ICPA. However, LG&E and KU will be obligated to pay monthly minimum demand charges over the life of the amended contract. The

[2] URS Corporation performed the original assessment in 2004 and completed an update during the pendency of this proceeding.

effectiveness of the amended ICPA is contingent upon all owners receiving the necessary regulatory approvals of the states in which they operate, if applicable.[3]

The Commission, having considered the evidence of record and being otherwise sufficiently advised, finds that the energy available from OVEC is a cost-effective source of energy to LG&E and KU, and it is reasonable for LG&E and KU to secure a portion of this available energy. We further find that LG&E's and KU's participation in the OVEC contract is for lawful objects within the corporate purposes of LG&E's and KU's utility operations, is necessary and appropriate for and consistent with the proper performance of their service to the public, will not impair their ability to perform that service, is reasonably necessary and appropriate for such purposes, and should therefore be approved.

IT IS THEREFORE ORDERED that:

1. LG&E and KU are authorized to enter into the Amended Inter-Company Power Agreement among OVEC and its owners as set forth in the provisions and terms in their applications.

2. After the Amended Inter-Company Power Agreement has received all necessary regulatory approvals, LG&E and KU shall, within 20 days of the finalization of the Amended Inter-Company Power Agreement, file a copy of the agreement with the Commission.

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[3] In addition to other state commissions, the investor-owned OVEC owners must also receive consent, or approval, of the Federal Energy Regulatory Commission.

Nothing contained herein shall be construed as a finding of value for any purpose or as a warranty on the part of the Commonwealth of Kentucky or any agency thereof as to the securities authorized herein.

By the Commission

ENTERED

AUG 11 2011

KENTUCKY PUBLIC SERVICE COMMISSION

ATTEST:

Executive Director

Case No. 2011-00099
Case No. 2011-00100

Robert M Conroy
Director, Rates
Louisville Gas and Electric Company
220 W. Main Street
P. O. Box 32010
Louisville, KY 40202

JIF-05

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

In re:	)	Chapter 11
	)	
FIRSTENERGY SOLUTIONS CORP., *et al.*,[1]	)	Case No. 18-50757 (AMK)
	)	(Jointly Administered)
Debtors.	)	
	)	Hon. Judge Alan M. Koschik
	)	

STIPULATION

FirstEnergy Solutions Corp. ("FES") and FirstEnergy Generation, LLC ("FG" and together with FES, "Movants"), together with the Ohio Valley Electric Corporation ("OVEC"), Duke Energy Ohio, Inc. ("Duke"), and the Office of the Ohio Consumers' Counsel (the "OCC," and together with OVEC and Duke, the "Objectors"), jointly submit this Stipulation in connection with and solely for the purposes of the *Motion for Entry of an Order Authorizing FirstEnergy Solutions Corp. and FirstEnergy Generation, LLC to Reject a Certain Multi-Party Intercompany Power Purchase Agreement With the Ohio Valley Electric Corporation* [Docket No. 44] (the "OVEC ICPA Rejection Motion").[2] **Absent agreement of the parties, this Stipulation may not be used or introduced in any other administrative or judicial proceeding, including, but not limited to, any proceeding before the Public Utilities Commission of Ohio or the Federal Energy Regulatory Commission. Nothing set forth in**

[1] The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's federal tax identification number, are: FE Aircraft Leasing Corp. (9245), case no. 18-50759; FirstEnergy Generation, LLC (0561), case no. 18-50762; FirstEnergy Generation Mansfield Unit 1 Corp. (5914), case no. 18-50763; FirstEnergy Nuclear Generation, LLC (6394), case no. 18-50760; FirstEnergy Nuclear Operating Company (1483), case no. 18-50761; FirstEnergy Solutions Corp. (0186); and Norton Energy Storage L.L.C. (6928), case no. 18-50764. The Debtors' address is: 341 White Pond Dr., Akron, OH 44320.

[2] Capitalized terms not defined herein are defined in the OVEC ICPA Rejection Motion.

this Stipulation shall constitute an admission or a waiver of: (1) the right of any party to dispute and/or take discovery respecting the facts set forth herein following the hearing on the OVEC ICPA Rejection Motion to the extent relevant to matters remaining in dispute; or (2) any claim, defense, argument, or position of any party with respect to (a) any subsequent appeal of any Order granting the OVEC ICPA Rejection Motion or post-appellate hearings; (b) the Debtors' request for *nunc pro tunc* relief with respect to the effective date the OVEC ICPA shall be deemed rejected; (c) the calculation of OVEC's claim against FES for rejection damages; or (d) any proceeding outside of the contested matter associated with the OVEC ICPA Rejection Motion.

1. FES is an Ohio-based power company and a wholly-owned subsidiary of non-Debtor FirstEnergy Corp. ("FE Corp."). FES provides energy-related products and services to retail and wholesale customers. FES owns and operates, through its subsidiary FirstEnergy Generation, LLC ("FG"), certain fossil-generating facilities. FES also owns nuclear-generating facilities through its subsidiary FirstEnergy Nuclear Generation, LLC ("NG"), which are operated by Debtor FirstEnergy Nuclear Operating Company ("FENOC"). FES purchases the entire output of both FG and NG, as well as the output of other FE Corp. subsidiaries, and sells that output to one or more regional transmission organizations, principally PJM Interconnection LLC ("PJM"). This represents the great majority of FES's power purchases and sales, totaling close to 10,000 megawatts ("MWs") of capacity, and generation of 52 terawatt hours ("TWh") in 2017.

2. FES is party to a multi-party intercompany power agreement pursuant to which FES and several other power companies have the right to purchase power from OVEC (the "OVEC ICPA"). OVEC, together with its wholly-owned subsidiary, Indiana-

Kentucky Electric Corporation ("IKEC"), are an investor-owned utility that operates two coal-fired power plants—the Kyger Creek plant in Cheshire, Ohio and the Clifty Creek plant in Madison, Indiana (the "Power Stations")—as well as transmission facilities through which it connects and transmits power to its various constituents.

3. OVEC and IKEC were formed on October 1, 1952 to provide electric power in support of the operation of uranium enrichment facilities then under construction by the Atomic Energy Commission (the "AEC") near Portsmouth, Ohio (the "Portsmouth Facilities"). The AEC's facilities are now operated by its successor agency, the Department of Energy ("DOE"). On October 15, 1952, OVEC and the AEC entered into a power supply agreement supporting the AEC's Portsmouth facilities (the "DOE Power Agreement"). On July 10, 1953, OVEC and fifteen public utility companies (each, an "Original Sponsoring Company") entered into the OVEC ICPA. The OVEC ICPA was executed to support the DOE Power Agreement and provide for excess energy sales to the Original Sponsoring Companies of power and energy not utilized by DOE or its predecessors.

4. On September 29, 2000, DOE notified OVEC of its cancellation of the DOE Power Agreement, effective April 30, 2003. The OVEC ICPA, and all of the amendments thereto, collectively constitute a cost-sharing agreement of delineated costs based upon each company's power participation ratio (defined below).

5. The OVEC ICPA was subsequently amended and restated in its entirety, first on March 13, 2006, and again on September 10, 2010. The current term of the OVEC ICPA extends through June 30, 2040.

6. As with prior iterations of the OVEC ICPA, on March 23, 2011, OVEC filed the current OVEC ICPA with the Federal Energy Regulatory Commission ("FERC"), initiating a proceeding captioned *Ohio Valley Elec. Corp.*, Docket No.s ER11-3181-000, ER11-3440-000, ER11-3441-0000. Notice of the OVEC ICPA's filing was published in the Federal Register. In accordance with the Code of Federal Regulations, FERC set a deadline by which interested parties could intervene, protest, or otherwise comment on the filed OVEC ICPA. No protests or comments were received. FERC accepted the filed OVEC ICPA in a delegated letter order issued on May 23, 2011. As provided in the letter order, the OVEC ICPA was "accepted for filing, effective May 23, 2011," and the "order constitutes final agency action." The OVEC ICPA governs the rates, terms, and conditions of wholesale sales of electricity.

7. Under the OVEC ICPA, all of the delineated costs associated with OVEC's operation are collectively allocated to all of the Sponsoring Companies based upon their power participation ratios (defined below).

8. The current parties to the OVEC ICPA (the "Sponsoring Companies") are listed in the chart below, and are each assigned a "Power Participation Ratio," which dictates the allocation of corresponding benefits and related payment obligations under the OVEC ICPA:

Sponsoring Company	% Share
Allegheny Energy Supply Company L.L.C.	3.01%
Appalachian Power Company	15.69%
Buckeye Power Generating, LLC	18.00%
The Dayton Power and Light Company	4.90%

Duke Energy Ohio, Inc.	9.00%
FirstEnergy Solutions Corp.	4.85%
Indiana Michigan Power Company	7.85%
Kentucky Utilities Company	2.50%
Louisville Gas and Electric Company	5.63%
Monongahela Power Company	0.49%
Ohio Power Company	19.93%
Peninsula Generation Cooperative	6.65%
Southern Indiana Gas and Electric Company	1.50%
Total:	100.00%

9. Pursuant to the terms of the OVEC ICPA, FES is responsible for its 4.85% share of all of OVEC's delineated costs and expenses, and is entitled to receive its 4.85% share of the available power and energy produced by the Power Stations. Last year, FES purchased approximately 0.6 TWh of power from OVEC under the OVEC ICPA.

10. On March 31, 2018 (the "Petition Date"), FES filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code. The next day, the Debtors filed the *Motion for Entry of an Order Authorizing FirstEnergy Solutions Corp. and FirstEnergy Generation, LLC to Reject a Certain Multi-Party Intercompany Power Purchase Agreement With the Ohio Valley Electric Corporation as of the Petition Date* [Docket No. 44] (the "OVEC ICPA Rejection Motion").

11. On July 13, 2018, the Court issued an Order (the "Interlocutory Order on Standard") providing, among other things, that it would apply the business judgment standard in adjudicating the OVEC ICPA Rejection Motion. Specifically, the Court determined that: 1) the business judgment standard shall govern the Court's

determination of whether the Debtors may reject the OVEC ICPA pursuant to 11 U.S.C. § 365; 2) in applying the business judgment standard, the Court will consider whether the OVEC ICPA is burdensome to the Debtors' estates and whether rejection of the OVEC ICPA will advance the Debtors' chapter 11 reorganization; and 3) the Court rejected any legal standard that would require consideration of anything other than whether rejection is consistent with the Debtors' sound business judgment. In the Interlocutory Order on Standard, the Court also incorporated by reference its findings and conclusions from the *Preliminary Injunction Against the Federal Energy Regulatory Commission* [Adv. Proc. Docket No. 114] (the "Preliminary Injunction Order") and the *Memorandum Decision Supporting Order Granting Preliminary Injunction* [Adv. Proc. Docket No. 125] (the "Memorandum Opinion").

12. FES asserts and has offered evidence that it has no need for the OVEC ICPA to reorganize. For purposes of this Stipulation for establishing the business judgment standard under 11 U.S.C. § 365 only, the Objectors do not contest that assertion.

13. FES also asserts and has offered evidence that the OVEC ICPA is burdensome to the Debtors' estates and that rejection of the OVEC ICPA will relieve it of near-term losses of at least $10 million on an annual average basis (2018 to 2023). Through discovery, OVEC has received and reviewed some of FES's underlying assumptions and projections for those projected losses. For purposes of this Stipulation for establishing the business judgment standard under 11 U.S.C. § 365 only, the Objectors do not contest FES's assertion that it will incur material, cumulative losses from its obligations under the OVEC ICPA and the resulting sale of capacity and energy in the PJM market in the near term. FES has also projected that it will continue to incur material losses under the

OVEC ICPA from 2022-2040. The Objectors take no position with respect to FES' assertions regarding the amount or duration of losses it may incur under the OVEC ICPA between 2018 and 2040.

14. The OVEC ICPA is an executory contract within the meaning of 11 U.S.C. § 365(a).

15. OVEC does not contest that FES's asserted projected near term losses and stated lack of need for the OVEC ICPA to reorganize are sufficient to meet the business judgment standard set by the Court in its Interlocutory Order on Standard.

16. OVEC agrees that to the extent the Court grants the OVEC ICPA Rejection Motion in a subsequent Order (the "Rejection Order") over OVEC's objection, it will not dispute that the rejection of the OVEC ICPA will be deemed effective no later than July 31, 2018 (the "Proposed Rejection Date"). For the avoidance of doubt, each party hereto agrees not to seek to appeal any forthcoming Order on the OVEC ICPA Rejection Motion on the ground that the facts herein did not support rejection under the standard articulated in the Interlocutory Order on Standard.

17. Subject to paragraph 19 of this Stipulation, upon the Bankruptcy Court granting the OVEC ICPA Rejection Motion, FES will have no obligation to either (a) take its previously applicable share of energy and capacity rights and obligations pursuant to the OVEC ICPA, or (b) offer any energy into PJM's energy market pursuant to the OVEC ICPA. FES and OVEC agree concurrently upon the execution of this Stipulation, and hereafter, to take commercially reasonable and good faith efforts to assist any interested Sponsoring Companies to (x) take a share, if any, of the energy and capacity rights and obligations previously committed to FES under the OVEC ICPA, and (y) be able to

continue to offer such energy into PJM's energy market. To the extent the Court enters a Rejection Order, FES shall remit to OVEC an amount in cash equal to the sum of all energy and capacity revenue received from or credited by PJM on account of FES's portion of the energy and capacity under the OVEC ICPA for the period from the date of entry of such Rejection Order to the date on which PJM recognizes that the change in control over such power and energy under the OVEC ICPA for purposes of receiving payments from PJM has been transitioned from FES to OVEC or one or more of the non-Debtor Sponsoring Companies (such date, "Transition Date") within five (5) business days of the Transition Date; provided however, that to the extent any such revenue is received or credited from PJM after such date, then FES shall remit it to OVEC within five (5) business days of receipt by FES.

18. The Debtors reserve all rights with respect to their request for *nunc pro tunc* relief, and the parties agree that the agreement of the Debtors to bifurcate adjudication of the availability of *nunc pro tunc* relief shall not prejudice the Debtors' request for such relief and shall not be used by any other party in opposing such relief.

19. Nothing contained herein, or by counsel's agreement to the submission of this stipulation, shall waive any Objector's rights to argue on appeal that the Court and FERC exercise concurrent jurisdiction over the rejection of the OVEC ICPA. For the avoidance of doubt, the Objectors continue to assert that rejection of the OVEC ICPA cannot be effectuated unless and until this Court authorizes rejection under the Bankruptcy Code and FERC authorizes rejection under the FPA.

20. The OCC joins this Stipulation solely with respect to paragraphs 1, 2, 5, 10-15, 16, 18 and 19. The OCC is not joining the stipulation with respect to the remaining

paragraphs and is not bound in any way by the agreements of the other parties contained in these paragraphs.

RESPECTFULLY SUBMITTED:

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JIF-06

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF OHIO
AKRON DIVISION

In re:	)	Chapter 11
	)	
FIRSTENERGY SOLUTIONS CORP., *et al.*,[1]	)	Case No. 18-50757 (Request for Joint Administration Pending)
	)	
Debtors.	)	Hon. Judge Alan M. Koschik
	)	

MOTION FOR ENTRY OF
AN ORDER AUTHORIZING FIRSTENERGY SOLUTIONS CORP. AND
FIRSTENERGY GENERATION, LLC TO REJECT
A CERTAIN MULTI-PARTY INTERCOMPANY POWER PURCHASE AGREEMENT
WITH THE OHIO VALLEY ELECTRIC CORPORATION
AS OF THE PETITION DATE

[1]The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's federal tax identification number, are: FE Aircraft Leasing Corp. (9245), case no. 18-50759; FirstEnergy Generation, LLC (0561), case no. 18-50762; FirstEnergy Generation Mansfield Unit 1 Corp. (5914), case no. 18-50763; FirstEnergy Nuclear Generation, LLC (6394), case no. 18-50760; FirstEnergy Nuclear Operating Company (1483), case no. 18-50761; FirstEnergy Solutions Corp. (0186); and Norton Energy Storage L.L.C. (6928), case no. 18-50764. The Debtors' address is: 341 White Pond Dr., Akron, OH 44320.

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FirstEnergy Solutions Corp. ("FES") and FirstEnergy Generation, LLC ("FG," and together with FES, "Movants"), debtors in the above-captioned chapter 11 cases (together with their affiliated debtors, the "Debtors"), file this motion (the "Motion") for an order, substantially in the form attached hereto as Exhibit A (the "Order"), authorizing the Debtors to reject a certain multi-party intercompany power purchase agreement. In support of the Motion, the Movants incorporate by reference the *Declaration of Donald R. Schneider in Support of Chapter 11 Petitions and First Day Motions* (the "Schneider First Day Declaration"),[1] the *Declaration of Kevin T. Warvell in Support of the Motion to Reject* (the "Warvell Declaration"), the *Declaration of Judah L. Rose in Support of the Motion to Reject* (the "Rose Declaration"), and the *Declaration of David Gerhardt in Support of the Motion to Reject* (the "Gerhardt Declaration"). The Movants respectfully represent as follows:

JURISDICTION AND VENUE

1. The United States Bankruptcy Court for the Northern District of Ohio (the "Court") has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2).

2. Venue is proper in this district pursuant to 28 U.S.C. §§ 1408 and 1409.

3. The statutory bases for the relief requested in this Motion are sections 105(a), 365, 1107(a), and 1108 of title 11 of the United States Code (the "Bankruptcy Code") and rules 2002, 6006 and 9014 of the Federal Rules of Bankruptcy Procedure.

RELIEF REQUESTED

4. By this Motion, the Movants seek to reject an extraordinarily burdensome executory power purchase agreement, effective as of the Petition Date (defined below). During

[1] Capitalized terms not defined herein are defined in the First Day Declaration.

2017 this contract—combined with nine[2] other power purchase agreements the Movants separately seek to reject—accounted for just approximately 3% of the power FES bought and sold into the wholesale market. Yet movants are losing approximately $12 million per year, and are expected to lose $268 million over the remaining 22 years left on the OVEC ICPA (defined below).

5. The Movants further request that the Court grant the relief requested in this Motion without a further hearing on a final basis if no objection is timely filed and served. If any objection(s) to the Motion is timely and properly filed and served with respect to the multi-party intercompany power purchase agreement, the parties shall attempt to reach a consensual resolution of the objection. If the parties are unable to so resolve any objection, the Debtors request that the Court hear such objection at the final hearing on this Motion.

6. The Movants further request that the Court set the deadline by which time the counterparty to the executory power purchase agreement must file a proof of claim relating to the rejection of the executory power purchase agreement as the later of (a) the claims bar date established in the Debtors' chapter 11 cases and (b) thirty (30) days after the entry of an order granting the relief sought in the instant motion.

Background

7. On March 31, 2018 (the "Petition Date"), each of the Debtors filed a voluntary petition with the Court under chapter 11 of the Bankruptcy Code. The Debtors continue to operate their businesses and manage their property as debtors and debtors-in-possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. The Debtors have requested joint administration of these chapter 11 cases pursuant to Bankruptcy Rule 1015(b). The Court has

[2] This includes eight "renewable" energy bundled power purchase agreements and one nonrenewable power purchase agreement.

not appointed a trustee and the Office of the United States Trustee for the Northern District of Ohio (the "US Trustee") has not yet formed any official committees in these chapter 11 cases.

8. Non-Debtor FirstEnergy Corp. ("FE Corp."), an Ohio corporation, is the ultimate parent company for each of the Debtors in these chapter 11 cases and certain of FE Corp.'s non-Debtor affiliates (collectively, "FirstEnergy" or "FirstEnergy Group"). Debtor FirstEnergy Solutions Corp. ("FES"), an Ohio corporation, is the parent company for Debtors FE Aircraft Leasing Corp. ("FEALC"), an Ohio corporation, FirstEnergy Generation, LLC ("FG"), an Ohio limited liability company, and FirstEnergy Nuclear Generation, LLC ("NG"), an Ohio limited liability company. Debtor FG is the parent company for Debtors FirstEnergy Generation Mansfield Unit 1 Corp. ("FGMUC"), an Ohio corporation, and Norton Energy Storage L.L.C. ("NES"), a Delaware limited liability company.[3]

9. FES sells power and provides energy-related products and services to retail and wholesale customers primarily in Illinois, Maryland, Michigan, New Jersey, Ohio, and Pennsylvania.

10. FG owns and operates three fossil generation plants[4], two in Ohio and one in Pennsylvania.[5] Additionally, FG operates the fossil generation plant owned by non-Debtor Bay Shore Power Company.

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[3] FG also owns a 99% limited partnership interest in Nautica Phase 2 Limited Partnership, which has $10 million in outstanding debt.

[4] FG also owns a steam turbine and combustion turbine at the Bay Shore Power Plant in Oregon, OH and a combustion turbine at the Eastlake Plant in Eastlake, OH.

[5] FG owns and operates the W.H. Sammis Plant in Stratton, OH, which is composed of seven units and the West Lorain Plant in Lorain, OH, which is composed of six units that run on heating oil. FG operates the entire Bruce Mansfield Plant in Shippingport, PA, where it owns two of the three units. FG owns approximately 6.17% of Unit 1 of the Bruce Mansfield Plant while approximately 93.83% of Unit 1 is under a leasehold interest.

11. A detailed description of the Debtors' business, capital structure, and the events leading to the chapter 11 cases is fully set forth in the Schneider First Day Declaration filed contemporaneously herewith and incorporated by reference as if fully set forth herein.

I. Overview of the Debtors' Business Operations

12. FES offers energy-related products and services to retail and wholesale customers (the "Customers"). FES provides energy products and services to retail Customers under various provider-of-last-resort ("POLR"), shopping, competitive-bid and non-affiliated contractual obligations. FES also participates in deregulated energy markets in Ohio, Pennsylvania, Maryland, Michigan, New Jersey and Illinois, competing to: (1) provide retail generation service directly to end users; (2) provide wholesale generation service to utilities, municipalities and co-operatives, which, in turn, resell to end users; and (3) sell power and capacity in the wholesale market.

13. FES, along with its non-debtor, unregulated generation affiliate, Allegheny Energy Supply Company, LLC ("AE Supply"), constitutes FirstEnergy's Competitive Energy Services ("CES") segment. Of FirstEnergy's three reportable operating segments, only the CES segment contains Debtor entities.[6] The CES segment's operating results are derived primarily from electric generation sales less the related costs of electricity generation, including fuel, purchased power and net transmission and ancillary costs and capacity costs charged by regional

[6] FirstEnergy's Regulated Distribution segment distributes electricity to approximately six million customers within 65,000 square miles of Ohio, Pennsylvania, West Virginia, Maryland, New Jersey and New York through FirstEnergy's ten non-debtor operating companies. FirstEnergy's Regulated Transmission segment transmits electricity through transmission facilities owned and operated by American Transmission Systems, Incorporated and Trans-Allegheny Interstate Line Company, and certain of FirstEnergy's utilities. FirstEnergy derives its revenue for its Regulated Transmission segment primarily from transmission services provided to load-serving entities pursuant to the PJM Open Access Transmission Tariff.

transmission organizations (each, a "RTO") to deliver energy to the CES segment's Customers, as well as other operating and maintenance costs.

14. FES is party to various contracts (the "RTO Agreements") with RTOs, specifically PJM Interconnection, L.L.C. ("PJM") and the Midcontinent Independent System Operator, Inc. ("MISO"). RTOs are responsible for coordinating, controlling and monitoring a regional high-voltage transmission grid. They administer markets to ensure safe and reliable operation and delivery of electricity. On a real-time basis, the RTO ensures that sufficient generation capacity exists to meet Customers' needs. Through the RTO Agreements, FES has made commitments to use good utility practices to assist the RTOs in meeting their operational commitments. Additionally, RTOs require payment and collateral obligations pursuant to the RTO Agreements. FES collects fees for its generation and pays the RTOs for expenses incurred in serving its Customers. In the event of an energy shortage or capacity failure in the region, PJM or the relevant RTO will pay power providers to remain in operation either by actively producing power or remaining available to offer capacity. As a result of the role RTOs play in administering markets, no reliability concern (and therefore no issue for consumers) is implicated by a breach of the executory power purchase agreements. The counterparties can resell the energy, bring a claim for damages and, in the unlikely event that a breach results in the shutdown of a counterparty, the relevant RTO would step in to prevent a shortage. Since no reliability issue would result from the rejection of the executory power purchase agreements, they are truly no different from any long-term money losing contract.

II. The OVEC Intercompany Power Purchase Agreement

15. FG is a party to a multi-party intercompany power purchase agreement (the "OVEC ICPA,") pursuant to which FES and several other power companies "sponsor" and

purchase power generated by fossil fuel from the Ohio Valley Electric Corporation ("OVEC"). The OVEC ICPA obligates FG to purchase 4.85% of the power that OVEC's fossil-fuel plants generate at an uneconomic rate until either the year 2040 or until OVEC ceases to operate. Based on current expectations, FG will lose approximately $268 million on an undiscounted basis over the remaining term of the OVEC ICPA.

16. The Movants can operate their businesses without the OVEC ICPA.

17. None of the Debtors' Customers—or any consumer for that matter—will go without power or capacity if the Movants are permitted to reject the OVEC ICPA. In 2017, the power generated under the OVEC ICPA totaled 0.6 TWh—just 0.1% of the total 767 TWh generated from all power plants selling in PJM. Further, OVEC will be able to sell its power generated for FG to other wholesale purchasers or into the regional wholesale electric spot markets (in this case, the markets operated by PJM).

Basis for Relief

18. Section 365(a) of the Bankruptcy Code provides that a debtor-in-possession "subject to the court's approval, may . . . reject any executory contract or unexpired lease of the debtor." 11 U.S.C. § 365(a). "This provision allows a trustee to relieve the bankruptcy estate of burdensome agreements which have not been completely performed." *Stewart Title Guar. Co. v. Old Republic Nat'l Title Co.*, 83 F.3d 735, 741 (5th Cir. 1996) (citing *In re Murexco Petrol., Inc.*, 15 F.3d 60, 62 (5th Cir. 1994)). Bankruptcy courts have broad authority and considerable discretion under this provision. *See Class Five Nev. Claimants v. Dow Corning Corp. (In re Dow Corning Corp.)*, 280 F.3d 648, 656 (6th Cir. 2002).

19. The Supreme Court has recognized that "the authority to reject an executory contract" is not merely incidental, but rather it "is vital to the basic purpose of a Chapter 11 reorganization, because rejection can release the debtor's estate from burdensome obligations

that can impede a successful reorganization." *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 528 (1984). Courts have similarly held that "[t]he right of a debtor in possession to reject certain contracts is fundamental to the bankruptcy system because it provides a mechanism through which severe financial burdens may be lifted while the debtor attempts to reorganize." *Westbury Real Estate Ventures, Inc. v. Bradlees Stores, Inc. (In re Bradlees Stores, Inc.)*, 194 B.R. 555, 558 n.1 (Bankr. S.D.N.Y. 1996). Rejection of an executory contract under 11 U.S.C. § 365(a) constitutes a breach of the contract—not a modification or termination. *Osprey-Troy Officentre, LLC v. World All. Fin. Corp.*, 502 F. App'x 455, 456-57 (6th Cir. 2012); *see also In re N. Am. Royalties, Inc.*, 276 B.R. 860, 865 (Bankr. E.D. Tenn. 2002) ("Rejection is independent of the contract terms.").

20. Rejection is "vital" and "fundamental," because in many cases, the debtor could not emerge from bankruptcy as a going concern if it were forced to specifically perform under burdensome executory contracts. *Leasing Serv. Corp. v. First Tenn. Bank N.A.*, 826 F.2d 434, 436 (6th Cir. 1987) ("Rejection denies the right of the contracting creditor to require the bankrupt estate to specifically perform..."); *see also Midway Motor Lodge of Elk Grove v. Innkeepers Telemgmt. & Equip. Corp.*, 54 F.3d 406, 407 (7th Cir. 1995) ("Rejection avoids specific performance, but the debtor assumes a financial obligation equivalent to damages for breach of contract."); *Bradlees Stores*, 194 B.R. at 558 ("Specific performance should not be permitted where the remedy would in effect do what section 365 meant to avoid, that is, impose burdensome contracts on the debtors.") (quoting *In re Fleishman*, 138 B.R. 641, 648 (Bankr. D. Mass. 1992)).

21. The Bankruptcy Code permits the debtor to breach the burdensome contracts, transforming those obligations into a pre-petition claim for damages, which may be satisfied and

discharged together with all claims against the estate. *See* 11 U.S.C. § 365(g); *see also In re Richendollar*, No. 04-70774, 2007 WL 1039065 (Bankr. N.D. Ohio Mar. 31, 2007) ("The purpose of section 365(g) is to make clear that, under the doctrine of relation back, the other party to a contract that has not been assumed Section 365(g) is simply a general unsecured creditor.") (quoting 3 Collier on Bankruptcy § 365.09[1] (15th ed. 2006).

22. Rejection thereby allows for ratable treatment of a debtors' unsecured lenders/creditors and its counterparties on executory contracts. *In re Albrechts Ohio Inns, Inc.*, 152 B.R. 496, 501–02 (Bankr. S.D. Ohio 1993) (noting the business judgment rule is satisfied for rejection purposes where "rejection will result in benefit to the debtor's general unsecured creditors"). Here, ensuring ratable treatment amongst such parties is essential to an equitable outcome. Requiring the Debtors to perform the remaining up to 22 years of the OVEC ICPA (as opposed to rejection), thereby paying OVEC in full, would be incredibly unfair and inequitable.

A. Rejection of the OVEC ICPA is a Proper Exercise of the Debtors' Business Judgment

23. The "business judgment" standard applies to determine whether the rejection of an executory contract or unexpired lease should be authorized. *See Orion Pictures Corp. v. Showtime Networks, Inc. (In re Orion Pictures Corp.)*, 4 F.3d 1095, 1098-99 (2d Cir. 1993); *see also Bildisco*, 465 U.S. at 524 (acknowledging that business judgment is the "traditional" standard for rejection of executory contracts); *Phar-Mor, Inc. v. Strouss Bldg. Assocs.*, 204 B.R. 948, 951-52 (N.D. Ohio 1997) ("Whether an executory contract is 'favorable' or 'unfavorable' is left to the sound business judgment of the debtor."); *In re Fashion Two Twenty, Inc.*, 16 B.R. 784, 787 (Bankr. N.D. Ohio 1982) (adopting the business judgment standard as "the proper standard" to determine a motion for rejection).

24. Rejection of an executory contract is appropriate where such rejection would benefit the estate. *See In re Orion Pictures Corp.*, 4 F.3d at 1098-99; *Sharon Steel Corp. v. Nat'l Fuel Gas Distrib. Corp.*, 872 F.2d 36, 40 (3d Cir. 1989); *In re HQ Glob. Holdings*, 290 B.R. 507, 511 (Bankr. D. Del. 2003); *In re Pesce Baking Co., Inc.*, 43 B.R. 949, 956 (Bankr. N.D. Ohio 1984).

25. Thus, upon finding that FG has exercised their sound business judgment in determining that rejection of the OVEC ICPA is in the best interests of the Debtors, their creditors and all parties in interest, the Court should approve the rejection under section 365(a) of the Bankruptcy Code. *See, e.g., In re Level Propane Gases, Inc.*, 297 B.R. 503, 509 (Bankr. N.D. Ohio 2003) (granting rejection where debtors "set forth a sound business judgment"), *aff'd*, No. 02-16172, 2007 WL 1821723 (N.D. Ohio June 22, 2007); *In re Fashion Two Twenty, Inc.*, 16 B.R. at 787 (same). If a debtor's business judgment has been reasonably exercised, a court should approve the assumption or rejection of an executory contract. *See, e.g., Phar-Mor, Inc.*, 204 B.R. at 952 ("Courts should generally defer to a debtor's decision whether to reject an executory contract."); *Summit Land Co. v. Allen (In re Summit Land Co.)*, 13 B.R. 310, 315 (Bankr. D. Utah 1981) (holding that absent extraordinary circumstances, court approval of a debtor's decision to assume or reject an executory contract "should be granted as a matter of course").

26. Here, the OVEC ICPA Rejection Motion clearly reflects the sound exercise of the Debtors' business judgment. Under the OVEC ICPA, which is wholly unnecessary for FG's business, the Debtors are today paying more than double the market value of capacity and power, and are expected to for the remaining life of this executory contract. As discussed more fully in the Warvell Declaration, the Debtors and ICF conducted an analysis of the potential business

impact of continuing to perform under the OVEC ICPA and determined that such performance would serve to decimate the Debtors' finances, to the tune of $268 million. The Debtors, assisted by financial advisors at Alvarez & Marsal and energy industry consultants at ICF International, have concluded that without rejection of the OVEC ICPA the Debtors' ability to reorganize would be jeopardized and their estates would be irreparably damaged.

27. The U.S. Court of Appeals for the Fifth Circuit has suggested that rejection of a FERC-regulated contract under section 365 should be subject to a more rigorous standard than the business judgment standard because of the "public interest" in the "transmission and sale of electricity," including "the continuity of electrical service to the customers of public utilities," that is recognized in the Federal Power Act ("FPA"). *Mirant Corp. v. Potomac Elec. Power Co. (In re Mirant Corp.)*, 378 F.3d 511, 525 (5th Cir. 2004) (citing 16 U.S.C. § 824(a)). While the Fifth Circuit correctly decided the core jurisdictional issue (*i.e.*, that FERC-regulated contracts could be rejected in bankruptcy), its suggestion that the bankruptcy court should apply a heightened standard is wrong as a matter of law—especially in the circumstances now before the Court. Moreover, even if the standard outlined in *Mirant* was deemed applicable here, the Movants would easily satisfy it.

28. The Fifth Circuit suggested that a debtor should be required to show that the contract "burdens the estate, that after careful scrutiny, the equities balance in favor of rejecting th[e] power contract, and that rejection of the contract would further the Chapter 11 goal of permitting the successful rehabilitation of debtors." *Id.* (citing *Bildisco*, 465 U.S. at 526-27).

29. There is no basis to apply a more rigorous standard than the business judgment standard to the OVEC ICPA. As explained above, the business judgment standard has long governed the rejection of executory contracts, except in a rare circumstance dictated by

Congressional intent that is not found in the FPA. In *Mirant*, the Fifth Circuit suggested without any basis in precedent that a more rigorous standard should apply to wholesale power contracts by analogizing those contracts to collective bargaining agreements subject to National Labor Relations Board regulation, which the Supreme Court held should be subject to more rigorous scrutiny because of the "special nature of a collective bargaining contract." *In re Mirant Corp.*, 378 F.3d at 524-25 (quoting *Bildisco*, 465 U.S. at 524). In *Bildisco*, however, appellate courts had applied different variations of a heightened standard prior to Congress's enactment of section 365(a), and the Court determined that "Congress intended" a higher standard to apply to collective bargaining contracts. *Bildisco*, 465 U.S. at 525-26. There is no evidence that Congress intended a more rigorous standard to apply to wholesale power contracts. And it is not sufficient to state that FERC-regulated contracts are important—so are many contracts in many important areas of the economy subject to federal regulation that are nonetheless governed by the business judgment standard. *See, e.g.*, *Grp. of Instl. Inv'rs v. Chi., M., St. P. & Pac. R.R. Co.*, 318 U.S. 523, 550 (1943) (railroad); *In re Trans World Airlines, Inc.*, 261 B.R. 103, 123 (Bankr. D. Del. 2001) (aviation); *In re Enron Corp.*, No. 01 B 16034, 2006 WL 898033, at *4 (Bankr. S.D.N.Y. Mar. 24, 2006) (telecom).

30. It is even more doubtful that Congress could have intended a more rigorous standard to apply to rejections by electricity *customers* (such as FES and FG as purchasers under the OVEC ICPA) given that the FPA was enacted to protect such customers, not regulate them—much less force them to continue purchasing electric service they neither need, want, or can afford. *Pa. Water & Power Co. v. Fed. Power Comm'n*, 343 U.S. 414, 418 (1952) ("A major purpose of the whole [Federal Power] Act is to protect power consumers against excessive prices."); *Cal. ex rel. Lockyer v. FERC*, 383 F.3d 1006, 1017 (9th Cir. 2004) (describing

"protecting consumers" as the FPA's "primary purpose"). In sum, there is no heightened or otherwise different bankruptcy-related standard applying to wholesale electric contracts. Nothing in the text of the FPA states or implies such a standard. No Supreme Court case suggests such a standard. And no case actually *applies* such a standard, as *Mirant* was decided on other grounds on remand.

31. Even if the Court determined that the heightened standard suggested by the Fifth Circuit should apply, however, Debtors would clearly meet it. The OVEC ICPA is extremely burdensome to Debtors' estates, and the cost of continuing to perform under it would threaten the viability of Debtors' restructuring efforts. And importantly, the public interest in "continuity of electrical service" is not implicated by rejection of the OVEC ICPA because rejection would not "cause any disruption in the supply of electricity to other public utilities or to consumers." *In re Mirant*, 378 F.3d at 525. As noted above, FES and FG are not electric suppliers under the OVEC ICPA; they are customers. Their rejection of the OVEC ICPA therefore will not cause any "disruption in the supply of electricity" because FES and FG do not supply electricity under these contracts in the first instance. Put simply, no customers will have their power supply threatened as a result of the Movants' rejection of the OVEC ICPA.

32. Rejection of the OVEC ICPA will relieve the Movants of the near term losses of approximately $12 million on an annual average basis (2018 to 2023) and will eliminate the approximately $268 million in continuing losses over the remaining life of the contracts. Rejection of the OVEC ICPA is thus a sound exercise of the Movants' business judgment and will benefit the Debtors' estates and their creditors.

B. This Court Should Grant the Requested Relief *Nunc Pro Tunc*

33. The Movants request that the Court deem the rejection, if granted, to have retroactive effect to the date of the filing of this Motion on April 1, 2018. Under section 105 of

the Bankruptcy Code, the Court has expansive equitable powers to fashion any order or decree that is necessary to carry out the provisions of the Bankruptcy Code. 11 U.S.C. § 105(a). This includes a grant of *nunc pro tunc* relief on a debtor's motion to reject a lease, when such relief is equitable. *EOP-Colonnade of Dall. LP v. Faulkner (In re Stonebridge Techs., Inc.)*, 430 F.3d 260, 273 (5th Cir. 2005) (noting that "most courts have held that lease rejection may be retroactively applied"); *Pac. Shores Dev., LLC v. At Home Corp. (In re At Home Corp.)*, 392 F.3d 1064, 1071-72 (9th Cir. 2004) (affirming bankruptcy court's exercise of its equitable authority to approve retroactive rejection under section 365); *Thinking Machs. Corp. v. Mellon Fin. Servs. Corp. # 1 (In re Thinking Machs. Corp.)*, 67 F.3d 1021, 1028 (1st Cir. 1995) (recognizing that bankruptcy courts have discretion to approve rejection retroactive under section 365 "when the balance of the equities preponderates in favor of such remediation"); *see also In re QSL Medina, Inc.*, No. 15-52722 (AMK) (Bankr. N.D. Ohio Dec. 15, 2015), ECF No. 105 (authorizing rejection effective as of the petition date).

34. Courts determine whether retroactive effect is appropriate on a case-by case basis. *See In re Thinking Machs. Corp.*, 67 F.3d at 1029 n.9 ("[W]e eschew any attempt to spell out the range of circumstances that might justify the use of a bankruptcy court's equitable powers in this fashion. That exercise is best handled on a case-by-case basis.").

35. Here, equitable considerations support the retroactive rejection of the OVEC ICPA effective as of the Petition Date. First, the Court's decision whether to grant rejection on a *nunc pro tunc* basis has potentially significant consequences to the Debtors' estates. Performance under unprofitable, non-essential contracts such as the OVEC ICPA, for any period of time, even for a few months at a loss of about $1 million per month in the near term, will hamper the Debtors' efforts to maximize value and pursue a successful emergence from chapter

11. The Movants' continued performance under the OVEC ICPA would pose a substantial threat to a successful restructuring of the Debtors.

36. Finally, the Movants have not delayed in seeking to reject the OVEC ICPA, but moved for rejection immediately upon filing for chapter 11 relief. These facts support granting retroactive relief. *In re At Home Corp*., 392 F.3d at 1072-73 (granting retroactive effect in part because debtor filed its motion on the first day of the case and scheduled the hearing for the "earliest practicable date"). There is no legitimate basis for delaying rejection, and OVEC will suffer no material prejudice from a grant of retroactive relief.

Reservation of Rights

37. Nothing contained in this Motion or any actions taken by the Debtors pursuant to the relief granted in the Order is intended or should be construed as: (a) an admission as to the validity of any particular claim against a Debtor entity; (b) a waiver of the Debtors' rights to dispute any particular claim on any grounds; (c) a promise or requirement to pay any particular claim; (d) an implication or admission that any particular claim is of a type specified or defined in this Motion; (e) a request or authorization to assume any agreement, contract, or lease pursuant to 11 U.S.C. § 365; or (f) a waiver or limitation of any of Debtors' rights under the Bankruptcy Code or any other applicable law.

Notice

38. No trustee, examiner or official committee has been appointed in the Debtors' chapter 11 cases. Notice of this Motion has been served on the following parties and/or their counsel, if known, via facsimile, overnight delivery, regular U.S. Mail, e-mail, and/or hand delivery: (a) the Office of the U.S. Trustee for the Northern District of Ohio; (b) the entities listed on the Consolidated List of Creditors Holding the 50 Largest Unsecured Claims filed pursuant to Bankruptcy Rule 1007(d); (c) counsel to the Bank of New York Mellon Trust

Company, N.A., in its capacity as indenture trustee under various indenture agreements; (d) counsel to UMB Bank, National Association, in its capacity as indenture trustee, paying agent, and collateral trustee under various indenture agreements, including, without limitation, certain pollution control revenue bond indentures and certain first mortgage bond indentures, and trust agreements; (e) counsel to Wilmington Savings Fund Society, FSB, in its capacity as indenture trustee and pass through trustee under various indenture agreements and trust agreements in connection with the Bruce Mansfield Unit 1 sale-leaseback; (f) counsel to the Ad Hoc Group of Holders of the 6.85% Pass Through Certificates due 2034; (g) counsel to the ad hoc group of certain holders of (i) pollution control revenue bonds supported by notes issued by FG and NG and (ii) certain unsecured notes issued by FES (collectively, the "Ad Hoc Noteholder Group"); (h) counsel to FirstEnergy Corp.; (i) counsel to MetLife Capital, Limited Partnership; (j) the District Director of the Internal Revenue Service; (k) the Securities and Exchange Commission; (l) the Office of the United States Attorney for the Northern District of Ohio; (m) the United States Environmental Protection Agency; (n) the Nuclear Regulatory Commission; (o) the United States Department of Energy; (p) the Federal Energy Regulatory Commission; (q) the Office of the Attorney General for Ohio; (r) the Office of the Attorney General for Pennsylvania; (s) the Office of the Attorney General for Illinois; (t) the Office of the Attorney General for Maryland; (u) the Office of the Attorney General for Michigan; (v) the Office of the Attorney General for New Jersey; (w) the National Association of Attorneys General; and (x) the Ohio Valley Electric Corporation. The Debtors submit that, in light of the nature of the relief requested, no other or further notice need be given.

CONCLUSION

WHEREFORE, the Movants respectfully request that the Court enter an order granting the relief requested by this Motion and such further relief as may be just and necessary under the circumstances.

Dated: April 1, 2018

Respectfully submitted,

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Proposed Counsel for Debtors and Debtors in Possession

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF OHIO
AKRON DIVISION

In re:	)	Chapter 11
	)	
FIRSTENERGY SOLUTIONS CORP., *et al.*,[1]	)	Case No. 18-50757
	)	(Request for Joint Administration Pending)
Debtors.	)	
	)	Hon. Judge Alan M. Koschik
	)	

[PROPOSED] ORDER (I) AUTHORIZING THE DEBTORS TO REJECT CERTAIN A CERTAIN MULTI-PARTY INTERCOMPANY POWER PURCHASE AGREEMENT WITH THE OHIO VALLEY ELECTRIC CORPORATION *NUNC PRO TUNC* TO THE PETITION DATE AND (II) GRANTING CERTAIN RELATED RELIEF

Upon the motion of FirstEnergy Solutions Corp. ("FES") and FirstEnergy Generation, LLC ("FG,"), debtors in the above-captioned chapter 11 cases (together with their affiliated debtors the "Debtors"), for the entry of the Proposed Order (i) authorizing and approving the rejection, *nunc pro tunc* to the date of commencement of these chapter 11 cases, of a certain multi-party intercompany power purchase agreement with the Ohio Valley Electric Corporation (the "OVEC ICPA") and (ii) granting related relief; and the Court having jurisdiction to consider the motion and the relief requested therein in accordance with 28 U.S.C. § 1334; and consideration of the motion and the relief requested therein being a core proceeding in accordance with 28 U.S.C. §§ 157(b)(2); and venue being proper in this jurisdiction pursuant to

[1] The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's federal tax identification number, are: FE Aircraft Leasing Corp. (9245), case no. 18-50759; FirstEnergy Generation, LLC (0561), case no. 18-50762; FirstEnergy Generation Mansfield Unit 1 Corp. (5914), case no. 18-50763; FirstEnergy Nuclear Generation, LLC (6394), case no. 18-50760; FirstEnergy Nuclear Operating Company (1483), case no. 18-50761; FirstEnergy Solutions Corp. (0186); and Norton Energy Storage L.L.C. (6928), case no. 18-50764. The Debtors' address is: 341 White Pond Dr., Akron, OH 44320.

28 U.S.C. §§ 1408 and 1409; and due and proper notice of the motion being adequate and appropriate under the particular circumstances; and a hearing having been held to consider the relief requested in the motion; and upon the First Day Declaration, the record of the hearing and all proceedings had before the Court; and the Court having found and determined that the relief sought in the motion is in the best interests of the Debtors' estates, their creditors, and other parties in interest, and that the legal and factual bases set forth in the motion establish just cause for the relief granted herein; and any objections to the requested relief having been withdrawn or overruled on the merits; and after due deliberation and sufficient cause appearing therefor, it is hereby **ORDERED**:

1. The motion is granted to the extent set forth herein.

2. The OVEC ICPA is hereby rejected. Such rejection shall be effective *nunc pro tunc* to the Petition Date.

3. Any claims based on the rejection of the OVEC ICPA shall be filed in accordance with any applicable order establishing a bar date for filing proofs of claim in these cases, to be established by the Court at a later date.

4. Notwithstanding the relief granted herein and any actions taken hereunder, nothing contained in this Order shall constitute, nor is it intended to constitute, an admission as to the validity or priority of any claim against the Debtors, the creation of an administrative priority claim on account of the pre-petition obligations sought to be paid, or the assumption or adoption of any contract or agreement under Bankruptcy Code section 365.

5. Notice of the motion as provided herein shall be deemed good and sufficient and such notice satisfies the requirements of Bankruptcy Rule 6004(a) and the Local Rules.

6. Notwithstanding the possible applicability of Bankruptcy Rule 6004(h), this order shall be immediately effective and enforceable upon its entry.

7. The Debtors are authorized to take all actions necessary to effectuate the relief granted pursuant to this order.

SUBMITTED BY:

/s/

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Proposed Counsel for Debtors
and Debtors in Possession

JIF-07

Ohio Valley Electric Corporation and Subsidiary Company

Consolidating Financial Statements as of and for the Years Ended December 31, 2017 and 2016, and Independent Auditors' Report

Deloitte.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Ohio Valley Electric Corporation:

We have audited the accompanying consolidating financial statements of Ohio Valley Electric Corporation and its subsidiary company, Indiana-Kentucky Electric Corporation (the "Companies"), which comprise the consolidating balance sheets as of December 31, 2017 and 2016, and the related consolidating statements of income and retained earnings and cash flows for the years then ended, and the related notes to the consolidating financial statements.

Management's Responsibility for the Consolidating Financial Statements

Management is responsible for the preparation and fair presentation of these consolidating financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidating financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidating financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidating financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidating financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidating financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Companies' preparation and fair presentation of the consolidating financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Companies' internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidating financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidating financial statements referred to above present fairly, in all material respects, the financial position of the Companies as of December 31, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

April 12, 2018

OHIO VALLEY ELECTRIC CORPORATION AND SUBSIDIARY COMPANY

CONSOLIDATING BALANCE SHEETS
AS OF DECEMBER 31, 2017 AND 2016

	2017				2016			
ASSETS	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation
ELECTRIC PLANT:								
At original cost	$ 2,782,873,612	$ -	$ 1,386,407,023	$ 1,396,466,589	$ 2,739,103,561	$ -	$ 1,361,028,710	$ 1,378,074,851
Less—accumulated provisions for depreciation	1,445,352,656	-	722,873,892	722,478,764	1,352,933,437	-	672,452,518	680,480,919
	1,337,520,956	-	663,533,131	673,987,825	1,386,170,124	-	688,576,192	697,593,932
Construction in progress	6,493,278	-	3,229,235	3,264,043	14,638,632	-	5,467,210	9,171,422
Total electric plant	1,344,014,234	-	666,762,366	677,251,868	1,400,808,756	-	694,043,402	706,765,354
INVESTMENTS AND OTHER:								
Investment in subsidiary company	-	(3,400,000)	3,400,000	-	-	(3,400,000)	3,400,000	-
Advances to subsidiary	-	(666,968,344)	666,968,344	-	-	(700,952,460)	700,952,460	-
Total investments and other	-	(670,368,344)	670,368,344	-	-	(704,352,460)	704,352,460	-
CURRENT ASSETS:								
Cash and cash equivalents	58,978,090	-	58,971,890	6,200	47,810,728	-	47,804,528	6,200
Accounts receivable	40,734,337	-	40,368,102	366,235	37,443,514	-	37,407,281	36,233
Fuel in storage	33,817,111	-	9,750,310	24,066,801	76,387,854	-	37,168,045	39,219,809
Emission allowances	355,852	-	355,852	-	872,920	-	872,920	-
Materials and supplies	38,445,277	-	22,307,369	16,137,908	34,857,142	-	20,959,606	13,897,536
Income taxes receivable	-	-	-	-	3,118,299	-	3,118,299	-
Property taxes applicable to future years	2,912,500	-	2,912,500	-	2,822,500	-	2,822,500	-
Prepaid expenses and other	2,051,978	-	1,110,703	941,275	1,998,372	-	1,036,926	961,446
Total current assets	177,295,145	-	135,776,726	41,518,419	205,311,329	-	151,190,105	54,121,224
REGULATORY ASSETS:								
Unrecognized postemployment benefits	3,865,985	-	2,569,375	1,296,610	4,273,382	-	2,502,691	1,770,691
Unrecognized pension benefits	37,249,847	-	21,172,813	16,077,034	37,128,152	-	20,658,104	16,470,048
Decommissioning and demolition	678,154	(3,823,282)	4,501,436	-	-	-	-	-
Total regulatory assets	41,793,986	(3,823,282)	28,243,624	17,373,644	41,401,534	-	23,160,795	18,240,739
DEFERRED CHARGES AND OTHER:								
Unamortized debt expense	327,610	-	327,610	-	498,536	-	498,536	-
Long-term investments	154,273,960	-	123,242,120	31,031,840	119,002,376	-	92,084,973	26,917,403
Income taxes receivable	9,294,909	-	9,294,909	-	-	-	-	-
Deferred tax assets	-	-	-	-	2,700,000	-	2,700,000	-
Other	1,534	-	550	984	78,637	-	77,653	984
Total deferred charges and other	163,898,013	-	132,865,189	31,032,824	122,279,549	-	95,361,162	26,918,387
TOTAL	$ 1,727,001,378	$ (674,191,626)	$ 1,634,016,249	$ 767,176,755	$ 1,769,801,168	$ (704,352,460)	$ 1,668,107,924	$ 806,045,704

(Continued)

OHIO VALLEY ELECTRIC CORPORATION AND SUBSIDIARY COMPANY

CONSOLIDATING BALANCE SHEETS
AS OF DECEMBER 31, 2017 AND 2016

	2017				2016			
CAPITALIZATION AND LIABILITIES	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation
CAPITALIZATION:								
Common stock, $100 par value—authorized, 300,000 shares; outstanding, 100,000 shares in 2017 and 2016	$ 10,000,000	$ -	$ 10,000,000	$ -	$ 10,000,000	$ -	$ 10,000,000	$ -
Common stock, without par value, stated at $200 per share—authorized, 100,000 shares; outstanding, 17,000 shares in 2017 and 2016	-	(3,400,000)	-	3,400,000	-	(3,400,000)	-	3,400,000
Long-term debt	1,261,297,697	-	1,261,297,697	-	1,170,781,545	-	1,170,781,545	-
Line of credit borrowings	85,000,000	-	85,000,000	-	85,000,000	-	85,000,000	-
Retained earnings	10,342,251	-	10,342,251	-	8,805,462	-	8,805,462	-
Total capitalization	1,366,639,948	(3,400,000)	1,366,639,948	3,400,000	1,274,587,007	(3,400,000)	1,274,587,007	3,400,000
CURRENT LIABILITIES:								
Current portion of long-term debt	76,483,805	-	76,483,805	-	248,483,907	-	248,483,907	-
Accounts payable	31,331,422	-	14,539,185	16,792,237	33,642,452	-	15,646,643	17,995,809
Accrued other taxes	10,799,150	-	7,240,498	3,558,652	9,858,927	-	6,401,108	3,457,819
Regulatory liabilities	1,909,470	-	1,904,265	5,205	11,610,328	-	4,981,503	6,628,825
Accrued interest and other	25,684,840	-	20,424,807	5,260,033	25,389,872	-	19,851,328	5,538,544
Total current liabilities	146,208,687	-	120,592,560	25,616,127	328,985,486	-	295,364,489	33,620,997
COMMITMENTS AND CONTINGENCIES (Notes 3, 9, 11, and 12)								
REGULATORY LIABILITIES:								
Postretirement benefits	56,495,826	-	42,087,129	14,408,697	32,986,336	-	27,632,746	5,353,590
Income taxes refundable to customers	11,571,428	-	11,571,428	-	5,433,716	-	5,433,716	-
Advance billing of debt reserve	30,000,000	-	30,000,000	-	-	-	-	-
Decommissioning and demolition	-	(3,823,282)	-	3,823,282	13,507,852	-	5,991,197	7,516,655
Total regulatory liabilities	98,067,254	(3,823,282)	83,658,557	18,231,979	51,927,904	-	39,057,659	12,870,245
OTHER LIABILITIES:								
Pension liability	37,249,847	-	21,172,813	16,077,034	37,128,152	-	20,658,104	16,470,048
Asset retirement obligations	57,170,620	-	29,218,810	27,951,810	33,044,921	-	13,813,296	19,231,625
Postretirement benefits obligation	17,196,685	-	9,658,850	7,537,835	39,218,090	-	21,536,990	17,681,100
Postemployment benefits obligation	3,865,985	-	2,569,375	1,296,610	4,273,382	-	2,502,691	1,770,691
Parent advances	-	(666,968,344)	-	666,968,344	-	(700,952,460)	-	700,952,460
Other non-current liabilities	602,352	-	505,336	97,016	636,226	-	587,688	48,538
Total other liabilities	116,085,489	(666,968,344)	63,125,184	719,928,649	114,300,771	(700,952,460)	59,098,769	756,154,462
TOTAL	$ 1,727,001,378	$ (674,191,626)	$ 1,634,016,249	$ 767,176,755	$ 1,769,801,168	$ (704,352,460)	$ 1,668,107,924	$ 806,045,704

See notes to consolidating financial statements.

(Concluded)

OHIO VALLEY ELECTRIC CORPORATION AND SUBSIDIARY COMPANY

CONSOLIDATING STATEMENTS OF INCOME AND RETAINED EARNINGS
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017				2016			
	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation
OPERATING REVENUES—Sales of electric energy to:								
Department of Energy	$ 8,187,803	$ -	$ 8,187,803	$ -	$ 8,519,114	$ -	$ 8,519,114	$ -
Ohio Valley Electric Corporation	-	(273,016,055)	-	273,016,055	-	(248,795,894)	-	248,795,894
Sponsoring Companies	615,870,005	-	615,870,005	-	577,376,640	-	577,376,640	-
Total operating revenues	624,057,808	(273,016,055)	624,057,808	273,016,055	585,895,754	(248,795,894)	585,895,754	248,795,894
OPERATING EXPENSES:								
Fuel and emission allowances consumed in operation	288,503,093	-	130,399,723	158,103,370	261,832,736	-	119,139,038	142,693,698
Purchased power	6,922,507	(273,016,055)	279,938,562	-	7,617,661	(248,795,894)	256,413,555	-
Other operation	85,206,695	-	53,496,374	31,710,321	78,388,622	-	46,417,345	31,971,277
Maintenance	82,862,095	-	42,309,172	40,552,923	81,651,038	-	40,877,037	40,774,001
Depreciation	84,699,703	-	42,969,917	41,729,786	73,882,917	-	43,669,797	30,213,120
Taxes—other than income taxes	11,975,463	-	6,962,589	5,012,874	11,983,295	-	6,512,648	5,470,647
Income taxes	-	-	-	-	345,420	-	345,420	-
Total operating expenses	560,169,556	(273,016,055)	556,076,337	277,109,274	515,701,689	(248,795,894)	513,374,840	251,122,743
OPERATING INCOME (LOSS)	63,888,252	-	67,981,471	(4,093,219)	70,194,065	-	72,520,914	(2,326,849)
OTHER INCOME (EXPENSE)	12,619,686	-	8,518,252	4,101,434	4,149,935	-	1,807,072	2,342,863
INCOME BEFORE INTEREST CHARGES	76,507,938		76,499,723	8,215	74,344,000	-	74,327,986	16,014
INTEREST CHARGES:								
Amortization of debt expense	3,479,683	-	3,479,683	-	4,618,191	-	4,618,191	-
Interest expense	71,491,466	-	71,483,251	8,215	68,787,341	-	68,771,327	16,014
Total interest charges	74,971,149	-	74,962,934	8,215	73,405,532	-	73,389,518	16,014
NET INCOME	1,536,789	-	1,536,789	-	938,468	-	938,468	-
RETAINED EARNINGS—Beginning of year	8,805,462	-	8,805,462	-	7,866,994	-	7,866,994	-
RETAINED EARNINGS—End of year	$ 10,342,251	$ -	$ 10,342,251	$ -	$ 8,805,462	$ -	$ 8,805,462	$ -

See notes to consolidating financial statements.

OHIO VALLEY ELECTRIC CORPORATION AND SUBSIDIARY COMPANY

CONSOLIDATING STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017				2016			
	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation
OPERATING ACTIVITIES:								
Net income	$ 1,536,789	$ -	$ 1,536,789	$ -	$ 938,468	$ -	$ 938,468	$ -
Adjustments to reconcile net income to net cash provided by (used in) operating activities:								
Depreciation	84,699,703	-	42,969,917	41,729,786	73,882,917	-	43,669,797	30,213,120
Amortization of debt expense	3,479,683	-	3,479,683	-	4,618,191	-	4,618,191	-
Deferred taxes/refundable taxes	-	-	-	-	3,539,704	-	3,539,704	-
Loss (gain) on marketable securities	(6,998,135)	-	(3,917,550)	(3,080,585)	655,288	-	2,157,082	(1,501,794)
Changes in assets and liabilities:								
Accounts receivable	(3,290,823)	-	(2,960,821)	(330,002)	(13,251,364)	-	(13,285,321)	33,957
Fuel in storage	42,570,743	-	27,417,735	15,153,008	4,974,911	-	(1,908,473)	6,883,384
Materials and supplies	(3,588,135)	-	(1,347,763)	(2,240,372)	(1,797,001)	-	(1,385,536)	(411,465)
Property taxes applicable to future years	(90,000)	-	(90,000)	-	27,500	-	27,500	-
Emissions allowances	517,068	-	517,068	-	(872,920)	-	(872,920)	-
Income tax receivable	(3,476,610)	-	(3,476,610)	-	(3,118,299)	-	(3,118,299)	-
Prepaid expenses and other	(53,606)	-	(73,777)	20,171	114,385	-	74,854	39,531
Other regulatory assets	(4,215,734)	-	(5,082,829)	867,095	(10,985,113)	-	(6,990,431)	(3,994,682)
Other noncurrent assets	77,103	-	77,103	-	(7,979)	-	(7,979)	-
Accounts payable	(2,476,932)	-	(1,292,910)	(1,184,022)	(955,698)	-	(1,852,001)	896,303
Accrued taxes	940,223	-	839,390	100,833	294,171	-	92,757	201,414
Accrued interest and other	294,968	-	573,479	(278,511)	3,434,977	-	1,747,215	1,687,762
Other liabilities	(20,444,880)	-	(10,576,173)	(9,868,707)	19,995,842	-	11,944,018	8,051,824
Other regulatory liabilities	52,091,672	-	51,029,772	1,061,900	(15,418,375)	-	(17,269,719)	1,851,344
Net cash provided by operating activities	141,573,097	-	99,622,503	41,950,594	66,069,605	-	22,118,907	43,950,698

(Continued)

OHIO VALLEY ELECTRIC CORPORATION AND SUBSIDIARY COMPANY

CONSOLIDATING STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017				2016			
	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation	Consolidated	Eliminations (Deduct)	Ohio Valley Electric Corporation	Indiana-Kentucky Electric Corporation
INVESTING ACTIVITIES:								
Changes in short-term intercompany lendings	$ -	$ (33,984,116)	$ 33,984,116	$ -	$ -	$ (27,728,795)	$ 27,728,795	$ -
Electric plant additions	(17,028,105)	-	(10,197,733)	(6,830,372)	(27,580,471)	-	(12,461,687)	(15,118,784)
Proceeds from sale of long-term investments	55,607,351	-	52,240,377	3,366,974	47,626,573	-	37,803,917	9,822,656
Purchases of long-term investments	(83,880,802)	-	(79,479,975)	(4,400,827)	(47,524,131)	-	(36,836,183)	(10,687,948)
Net cash (used in) provided by investing activities	(45,301,556)	(33,984,116)	(3,453,215)	(7,864,225)	(27,478,029)	(27,728,795)	16,234,842	(15,984,076)
FINANCING ACTIVITIES:								
Changes in short-term intercompany borrowings	-	33,984,116	-	(33,984,116)	-	27,728,795	-	(27,728,795)
Debt issuance and maintenance costs	(11,308,531)	-	(11,308,531)	-	(3,905,669)	-	(3,905,669)	-
Repayment of Senior 2006 Notes	(19,636,354)	-	(19,636,354)	-	(18,539,255)	-	(18,539,255)	-
Repayment of Senior 2007 Notes	(13,920,909)	-	(13,920,909)	-	(13,130,063)	-	(13,130,063)	-
Repayment of Senior 2008 Notes	(14,926,913)	-	(14,926,913)	-	(13,990,154)	-	(13,990,154)	-
Redemption of 2009 Bonds	(25,000,000)	-	(25,000,000)	-	-	-	-	-
Proceeds from line of credit	50,000,000	-	50,000,000	-	69,000,000	-	69,000,000	-
Payments on line of credit	(50,000,000)	-	(50,000,000)	-	(29,000,000)	-	(29,000,000)	-
Principal payments under capital leases	(311,472)	-	(209,219)	(102,253)	(508,280)	-	(270,453)	(237,827)
Net cash (used in) provided by financing activities	(85,104,179)	33,984,116	(85,001,926)	(34,086,369)	(10,073,421)	27,728,795	(9,835,594)	(27,966,622)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	11,167,362	-	11,167,362	-	28,518,155	-	28,518,155	-
CASH AND CASH EQUIVALENTS—Beginning of year	47,810,728	-	47,804,528	6,200	19,292,573	-	19,286,373	6,200
CASH AND CASH EQUIVALENTS—End of year	$ 58,978,090	$ -	$ 58,971,890	$ 6,200	$ 47,810,728	$ -	$ 47,804,528	$ 6,200
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:								
Interest paid	$ 72,541,166	$ -	$ 72,541,166	$ -	$ 69,458,491	$ -	$ 69,458,491	$ -
Income taxes (received) paid — net	$ (2,912,531)	$ -	$ (2,912,531)	$ -	$ (76,578)	$ -	$ (76,578)	$ -
Non-cash electric plant additions included in accounts payable at December 31	$ 746,202	$ -	$ 519,338	$ 226,864	$ 268,828	$ -	$ 124,667	$ 144,161

See notes to consolidating financial statements.

(Concluded)

OHIO VALLEY ELECTRIC CORPORATION AND SUBSIDIARY COMPANY

NOTES TO CONSOLIDATING FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Consolidating Financial Statements—The consolidating financial statements include the accounts of Ohio Valley Electric Corporation (OVEC) and its wholly owned subsidiary, Indiana-Kentucky Electric Corporation (IKEC), collectively, the Companies. All intercompany transactions have been eliminated in consolidation.

Organization—The Companies own two generating stations located in Ohio and Indiana with a combined electric production capability of approximately 2,256 megawatts. OVEC is owned by several investor-owned utilities or utility holding companies and two affiliates of generation and transmission rural electric cooperatives. These entities or their affiliates comprise the Sponsoring Companies. The Sponsoring Companies purchase power from OVEC according to the terms of the Inter-Company Power Agreement (ICPA), which has a current termination date of June 30, 2040. Approximately 27% of the Companies' employees are covered by a collective bargaining agreement that expires on August 31, 2018.

Prior to 2004, OVEC's primary commercial customer was the U.S. Department of Energy (DOE). The contract to provide OVEC-generated power to the DOE was terminated in 2003 and all obligations were settled at that time. Currently, OVEC has an agreement to arrange for the purchase of power (Arranged Power), under the direction of the DOE, for resale directly to the DOE. The agreement with the DOE expires on July 31, 2018. All purchase costs are billable by OVEC to the DOE.

Rate Regulation—The proceeds from the sale of power to the Sponsoring Companies are designed to be sufficient for OVEC to meet its operating expenses and fixed costs, as well as earn a return on equity before federal income taxes. In addition, the proceeds from power sales are designed to cover debt amortization and interest expense associated with financings. The Companies have continued and expect to continue to operate pursuant to the cost plus rate of return recovery provisions at least to June 30, 2040, the date of termination of the ICPA. However, in 2014 the Companies reduced their billings under the ICPA to effectively forego recovery of the equity return through the ICPA billings.

On March 31, 2018, one of the Sponsoring Companies filed for Chapter 11 bankruptcy protection. OVEC made a preemptive filing on March 26, 2018, with the Federal Energy Regulatory Commission (FERC) to request FERC take exclusive jurisdiction over the possible rejection of the ICPA in regards to the potential bankruptcy of this Sponsoring Company. On April 1, 2018, the Sponsoring Company filed a motion to reject the ICPA; however, no decision by the courts have been taken on this rejection motion to date. This Sponsoring Company's ownership and power participating benefits and requirements are approximately 5%. However, the Companies currently have access to the credit markets to fund ongoing liquidity needs, and the Sponsoring Companies remain obligated to fund debt service payments when due.

The accounting guidance for Regulated Operations provides that rate-regulated utilities account for and report assets and liabilities consistent with the economic effect of the way in which rates are established, if the rates established are designed to recover the costs of providing the regulated service and it is probable that such rates can be charged and collected. The Companies follow the accounting and reporting requirements in accordance with the guidance for Regulated Operations. Certain expenses and credits subject to utility regulation or rate determination normally reflected in income are deferred in the accompanying consolidating balance sheets and are recognized in income as the related amounts are included in service rates and recovered from or refunded to customers.

The Companies' regulatory assets, liabilities, and amounts authorized for recovery through Sponsor billings at December 31, 2017 and 2016, were as follows:

	2017		2016	
	OVEC	IKEC	OVEC	IKEC
Regulatory assets:				
Other assets:				
Unrecognized postemployment benefits	$ 2,569,375	$ 1,296,610	$ 2,502,691	$ 1,770,691
Unrecognized pension benefits	21,172,813	16,077,034	20,658,104	16,470,048
Asset retirement costs	4,501,436	-	-	-
Total	28,243,624	17,373,644	23,160,795	18,240,739
Total regulatory assets	$ 28,243,624	$ 17,373,644	$ 23,160,795	$ 18,240,739
Regulatory liabilities:				
Current liabilities:				
Deferred revenue—advances for construction	$ 140,021	$ 5,205	$ 3,094,147	$ 6,628,825
Deferred credit—advance collection of interest	1,764,244	-	1,887,356	-
Total	1,904,265	5,205	4,981,503	6,628,825
Other liabilities:				
Postretirement benefits	42,087,129	14,408,697	27,632,746	5,353,590
Income taxes refundable to customers	11,571,428	-	5,433,716	-
Advance billing of debt reserve	30,000,000	-	-	-
Decommissioning and demolition	-	3,823,282	5,991,197	7,516,655
Total	83,658,557	18,231,979	39,057,659	12,870,245
Total regulatory liabilities	$ 85,562,822	$ 18,237,184	$ 44,039,162	$ 19,499,070

Regulatory Assets—Regulatory assets consist primarily of pension benefit costs, postemployment benefit costs, and accrued decommissioning and demolition costs to be billed to the Sponsoring Companies in future years. The Companies' current billing policy for pension and postemployment benefit costs is to bill its actual plan funding.

Regulatory Liabilities—The regulatory liabilities classified as current in the accompanying consolidating balance sheet as of December 31, 2017, consist primarily of interest expense collected from customers in advance of expense recognition and customer billings for construction in progress. These amounts will be credited to customer bills during 2018. Other regulatory liabilities consist primarily of postretirement benefit costs and decommissioning and demolition costs that have been billed to customers in excess of cumulative expense recognition, income taxes refundable to customers that will be credited to bills over a long-term basis, and advanced billings collected from the Sponsoring Companies for debt services

In 2003, the DOE terminated the DOE Power Agreement with OVEC, entitling the Sponsoring Companies to 100% of OVEC's generating capacity under the terms of the ICPA. Under the terms of the DOE Power Agreement, OVEC was entitled to receive a "termination payment" from the DOE to recover unbilled costs upon termination of the agreement. The termination payment included unbilled postretirement benefit costs. In 2003, OVEC recorded a settlement payment of $97 million for the DOE obligation related to postretirement benefit costs. The regulatory liability for postretirement benefits recorded at December 31, 2017 and 2016, represents amounts collected in historical billings in excess of the accounting principles generally accepted in the United States of America (GAAP) net periodic benefit costs, including the DOE termination payment and incremental unfunded plan obligations recognized in the balance sheets but not yet recognizable in GAAP net periodic benefit costs. The Companies' ratemaking policy will recover postretirement benefits in an amount equal to estimated benefit accrual cost, plus amortization of unfunded liabilities, if any. As a result, related regulatory liabilities are being credited to customer bills on a long-term basis.

In January 2017, the Companies started advance billing the Sponsoring Companies for debt service as allowed under the ICPA. At December 31, 2017, $30 million had been advance billed to the Sponsoring Companies. As the Companies have not yet incurred these debt costs, a regulatory liability was recorded which will be credited to customer bills on a long-term basis.

Cash and Cash Equivalents—Cash and cash equivalents primarily consist of cash and money market funds and their carrying value approximates fair value. For purposes of these statements, the Companies consider temporary cash investments to be cash equivalents since they are readily convertible into cash and have original maturities of less than three months.

Electric Plant—Property additions and replacements are charged to utility plant accounts. Depreciation expense is recorded at the time property additions and replacements are billed to customers or at the date the property is placed in service if the in-service date occurs subsequent to the customer billing. Customer billings for construction in progress are recorded as deferred revenue—advances for construction. These amounts are closed to revenue at the time the related property is placed in service. Depreciation expense and accumulated depreciation are recorded when financed property additions and replacements are recovered over a period of years through customer debt retirement billing. All depreciable property will be fully billed and depreciated prior to the expiration of the ICPA. Repairs of property are charged to maintenance expense.

Fuel in Storage, Emission Allowances, and Materials and Supplies—The Companies maintain coal, reagent, and oil inventories, as well as emission allowances, for use in the generation of electricity for regulatory compliance purposes due to the generation of electricity. These inventories are valued at average cost, less reserves for obsolescence. Materials and supplies consist primarily of replacement parts necessary to maintain the generating facilities and are valued at average cost.

Long-Term Investments—Long-term investments consist of marketable securities that are held for the purpose of funding postretirement benefits, decommissioning and demolition costs, and debt service. These securities have been classified as trading securities in accordance with the provisions of the accounting guidance for Investments—Debt and Equity Securities. Trading securities reflected in Long-Term Investments are carried at fair value with the unrealized gain or loss, reported in Other Income (Expense). The cost of securities sold is based on the specific identification cost method. The fair value of most investment securities is determined by reference to currently available market prices. Where quoted market prices are not available, the Companies use the market price of similar types of securities that are traded in the market to estimate fair value. See Fair Value Measurements in Note 10. Due to tax limitations, the amounts held in the postretirement benefits portfolio have not yet been transferred to the Voluntary Employee Beneficiary Association (VEBA) trusts (see Note 8). Long-term investments primarily consist of municipal bonds, money market mutual fund investments, and mutual funds. Net unrealized gains (losses) recognized during 2017 and 2016 on securities still held at the balance sheet date were $6,995,056 and $(509,314), respectively.

Fair Value Measurements of Assets and Liabilities—The accounting guidance for Fair Value Measurements and Disclosures establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). Where observable inputs are available, pricing may be completed using comparable securities, dealer values, and general market conditions to determine fair value. Valuation models utilize various inputs that include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in inactive markets, and other observable inputs for the asset or liability.

Unamortized Debt Expense—Unamortized debt expense relates to costs incurred in connection with obtaining revolving credit agreements. These costs are being amortized over the term of the related revolving credit agreement and are recorded as an asset in the consolidating balance sheets. Costs incurred to issue debt are recorded as a reduction to long-term debt as presented in Note 6.

Asset Retirement Obligations and Asset Retirement Costs—The Companies recognize the fair value of legal obligations associated with the retirement or removal of long-lived assets at the time the obligations are incurred and can be reasonably estimated. The initial recognition of this liability is accompanied by a corresponding increase in depreciable electric plant. Subsequent to the initial recognition, the liability is adjusted for any revisions to the expected value of the retirement obligation (with corresponding adjustments to electric plant) and for accretion of the liability due to the passage of time.

These asset retirement obligations are primarily related to obligations associated with future asbestos abatement at certain generating stations and certain plant closure costs, including the impacts of the coal combustion residuals rule.

	OVEC	IKEC	Consolidated
Balance—January 1, 2016	$ 13,054,376	$ 18,195,463	$ 31,249,839
Accretion	778,726	1,054,033	1,832,759
Liabilities settled	(19,806)	(17,871)	(37,677)
Balance—December 31, 2016	13,813,296	19,231,625	33,044,921
Accretion	822,732	1,118,408	1,941,140
Liabilities settled	(19,806)	(25,232)	(45,038)
Revisions to cash flows	14,602,588	7,627,009	22,229,597
Balance—December 31, 2017	$ 29,218,810	$ 27,951,810	$ 57,170,620

During 2017, the Companies completed an updated study to estimate the asset retirement costs described above. The revised estimated costs are recorded in the accompanying balance sheets. Adjustments resulting from the revised estimated costs are included as revisions to cash flows in the above table. The increase in the asset retirement obligation is primarily the result of proposed regulations related to the disposal of coal combustion residuals, as further discussed in Note 9.

The Companies do not recognize liabilities for asset retirement obligations for which the fair value cannot be reasonably estimated. The Companies have asset retirement obligations associated with transmission assets at certain generating stations. However, the retirement date for these assets cannot be determined; therefore, the fair value of the associated liability currently cannot be estimated and no amounts are recognized in the consolidating financial statements herein.

Income Taxes—The Companies use the liability method of accounting for income taxes. Under the liability method, the Companies provide deferred income taxes for all temporary differences between the book and tax basis of assets and liabilities which will result in a future tax consequence. The Companies account for uncertain tax positions in accordance with the accounting guidance for Income Taxes.

Use of Estimates—The preparation of consolidating financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidating financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

New Accounting Pronouncements—In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers*. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. This standard also includes expanded disclosure requirements that result in an entity providing users of financial statements with comprehensive information about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. In August 2015, ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date,* was issued deferring the effective date of ASU 2014-09 to annual reporting periods beginning after December 15, 2018. The Companies plan to adopt the standard and all subsequent amendments in the fiscal year ending December 31, 2018. The Companies have not yet completed their evaluation of the impact of adopting the standard. The Companies' evaluation process will include, but is not limited to, identifying contracts within the scope of Topic 606 as well as evaluating the implications of specific contractual terms. The Companies expect the adoption of ASC 606 will not have a material impact on either the timing or amount of revenues recognized in their consolidating financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*, which represents a wholesale change to lease accounting. The standard introduces a lessee model that brings most leases into the balance sheet as well as aligns certain underlying principles of the new lessor model with those in Accounting Standards Codification (ASC) 606, *Revenue From Contracts With Customers*. In January 2018, the FASB issued ASU No. 2018-01, *Leases (Topic 842): Land Easements Practical Expedient for Transition to Topic 842*, which offers a practical expedient for accounting for land easements under ASU 2016-02. This practical expedient allows an entity the option of not evaluating existing land easements under ASC 842. New or modified land easements will still require evaluation under ASC 842 on a prospective basis beginning on the date of adoption. The Companies plan to adopt the new standard and all subsequent amendments in the fiscal year ending December 31, 2019. The Companies are in the process of evaluating the impact of adoption of this ASU on the Companies' consolidating financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The pronouncement changes the impairment model for most financial assets, replacing the current "incurred loss" model. ASU No. 2016-13 will require the use of an "expected loss" model for instruments measured at amortized cost and will also require entities to record allowances for available-for-sale debt securities rather than reduce the carrying amount. The Companies plan to adopt the standard for the fiscal year ended December 31, 2020. The Companies are in the process of evaluating the impact of adoption, if any, of this ASU on the **Companies' consolidating financial statements.**

Subsequent Events—In preparing the accompanying financial statements and disclosures, the Companies reviewed subsequent events through April 12, 2018, which is the date the consolidating financial statements were issued.

2. RELATED-PARTY TRANSACTIONS

Transactions with the Sponsoring Companies during 2017 and 2016 included the sale of all generated power to them, the purchase of Arranged Power from them, and other utility systems in order to meet the DOE's power requirements, contract barging services, railcar services, and minor transactions for services and materials. The Companies have Power Agreements with Louisville Gas and Electric Company, Duke Energy Ohio, Inc., The Dayton Power and Light Company, Kentucky Utilities Company, Ohio Edison Company, and American Electric Power Service Corporation as agent for the American Electric Power System Companies; and Transmission Service Agreements with Louisville Gas and Electric Company, Duke Energy Ohio, Inc., The Dayton Power and Light Company, The Toledo Edison Company, Ohio Edison Company, Kentucky Utilities Company, and American Electric Power Service Corporation as agent for the American Electric Power System Companies.

At December 31, 2017 and 2016, balances due from the Sponsoring Companies are as follows:

	2017	2016
Accounts receivable	$39,005,995	$36,035,316

During 2017 and 2016, American Electric Power accounted for approximately 44% of operating revenues from Sponsoring Companies and Buckeye Power accounted for 18%. No other Sponsoring Company accounted for more than 10%.

American Electric Power Company, Inc. and subsidiary company owned 43.47% of the common stock of OVEC as of December 31, 2017. The following is a summary of the principal services received from the American Electric Power Service Corporation as authorized by the Companies' Boards of Directors:

	2017	2016
General services	$ 3,787,293	$ 3,978,358
Specific projects	1,113,250	1,562,412
Total	$ 4,900,543	$ 5,540,770

General services consist of regular recurring operation and maintenance services. Specific projects primarily represent nonrecurring plant construction projects and engineering studies, which are approved by the Companies' Boards of Directors. The services are provided in accordance with the service agreement dated December 15, 1956, between the Companies and the American Electric Power Service Corporation.

3. COAL SUPPLY

The Companies have coal supply agreements with certain nonaffiliated companies that expire at various dates from the year 2018 through 2021. Pricing for coal under these contracts is subject to contract provisions and adjustments. The Companies currently have approximately 87% of their 2018 coal requirements under contract. These contracts are based on rates in effect at the time of contract execution.

4. ELECTRIC PLANT

Electric plant at December 31, 2017 and 2016, consists of the following:

	2017		2016	
	OVEC	IKEC	OVEC	IKEC
Steam production plant	$ 1,322,561,929	$ 1,366,250,783	$ 1,297,000,985	$ 1,348,646,702
Transmission plant	51,994,163	29,196,784	52,050,044	28,409,127
General plant	11,832,007	1,011,382	11,958,757	1,011,382
Intangible	18,924	7,640	18,924	7,640
	1,386,407,023	1,396,466,589	1,361,028,710	1,378,074,851
Less accumulated depreciation	722,873,892	722,478,764	672,452,518	680,480,919
	663,533,131	673,987,825	688,576,192	697,593,932
Construction in progress	3,229,235	3,264,043	5,467,210	9,171,422
Total electric plant	$ 666,762,366	$ 677,251,868	$ 694,043,402	$ 706,765,354

All property additions and replacements are fully depreciated on the date the property is placed in service, unless the addition or replacement relates to a financed project. As the Companies' policy is to bill in accordance with the debt service schedule under the debt agreements, all financed projects are being depreciated in amounts equal to the principal payments on outstanding debt.

5. BORROWING ARRANGEMENTS AND NOTES

OVEC has an unsecured bank revolving line of credit agreement with a borrowing limit of $200 million as of December 31, 2017 and 2016. The $200 million line of credit has an expiration date of November 14, 2019. At December 31, 2017 and 2016, OVEC had borrowed $85 million under this line of credit. Interest expense related to line of credit borrowings was $2,680,713 in 2017 and $1,692,301 in 2016. During 2017 and 2016, OVEC incurred annual commitment fees of $304,448 and $335,376, respectively, based on the borrowing limits of the line of credit.

6. LONG-TERM DEBT

The following amounts were outstanding at December 31, 2017 and 2016:

	Interest Rate	2017	2016
Senior 2006 Notes:			
2006A due February 15, 2026	5.80 %	$ 209,037,387	$ 227,600,578
2006B due June 15, 2040	6.40 %	56,503,080	57,576,242
Senior 2007 Notes:			
2007A-A due February 15, 2026	5.90 %	93,609,630	102,311,927
2007A-B due February 15, 2026	5.90 %	23,574,667	25,766,254
2007A-C due February 15, 2026	5.90 %	23,762,382	25,971,422
2007B-A due June 15, 2040	6.50 %	28,209,392	28,752,657
2007B-B due June 15, 2040	6.50 %	7,104,257	7,241,073
2007B-C due June 15, 2040	6.50 %	7,160,825	7,298,730
Senior 2008 Notes:			
2008A due February 15, 2026	5.92 %	29,219,169	31,932,971
2008B due February 15, 2026	6.71 %	59,238,453	64,641,227
2008C due February 15, 2026	6.71 %	61,136,357	66,463,125
2008D due June 15, 2040	6.91 %	41,017,439	41,752,834
2008E due June 15, 2040	6.91 %	41,730,140	42,478,312
Series 2009 Bonds:			
2009A due February 1, 2026	-	-	25,000,000
2009B due February 1, 2026	2.85 %	25,000,000	25,000,000
2009C due February 1, 2026	2.85 %	25,000,000	25,000,000
2009D due February 1, 2026	0.85 %	25,000,000	25,000,000
2009E due October 1, 2019	5.63 %	100,000,000	100,000,000
Series 2010 Bonds:			
2010A due February 1, 2040	5.57 %	50,000,000	50,000,000
2010B due February 1, 2040	2.85 %	50,000,000	50,000,000
Series 2012 Bonds:			
2012A due June 1, 2032	5.00 %	76,800,000	76,800,000
2012A due June 1, 2039	5.00 %	123,200,000	123,200,000
2012B due June 1, 2040	5.57 %	50,000,000	50,000,000
2012C due June 1, 2040	5.57 %	50,000,000	50,000,000
Series 2013 Notes:			
2013A due February 15, 2018	-	-	100,000,000
Series 2017 Notes:			
2017A due August 4, 2022	5.57 %	100,000,000	-
Total debt		1,356,303,178	1,429,787,352
Total premiums and discounts (net)		(483,065)	(505,664)
Less unamortized debt expense		(18,038,611)	(10,016,236)
Total debt net of premiums, discounts, and unamortized debt expense		1,337,781,502	1,419,265,452
Current portion of long-term debt		76,483,805	248,483,907
Total long-term debt		$ 1,261,297,697	$ 1,170,781,545

All of the OVEC amortizing unsecured senior notes have maturities scheduled for February 15, 2026, or June 15, 2040, as noted in the previous table.

During 2009, OVEC issued a series of four $25 million variable-rate non-amortizing tax-exempt pollution control bonds (2009A, B, C, and D Bonds) and $100 million fixed-rate non-amortizing tax-exempt pollution control bonds (2009E Bonds). The variable rates listed above reflect the interest rate in effect at December 31, 2017.

The 2009 Series D Bonds are secured by irrevocable transferable direct-pay letters of credit, expiring on November 14, 2019, issued for the benefit of the owners of the bonds. The interest rate on the bonds is adjusted weekly, and bondholders may require repurchase of the bonds at the time of such interest rate adjustments. OVEC has entered into an agreement to provide for the remarketing of the bonds if such repurchase is required. The 2009D Series Bonds are current, as they are redeemable at the election of the holders at any time. The 2009 Series B and C Bonds were remarketed in August 2016 for a five-year interest period that extends to August 25, 2021. The 2009A Bonds were secured by an irrevocable transferable direct-pay letter of credit at December 31, 2016, but were repurchased by OVEC on February 6, 2017 and are held by OVEC.

In December 2010, OVEC established a borrowing facility under which OVEC borrowed, in 2011, $100 million remarketable variable-rate bonds due on February 1, 2040. In June 2011, the $100 million variable-rate bonds were issued as two $50 million non-amortizing pollution control revenue bonds (Series 2010A and 2010B) with initial interest periods of three years and five years, respectively. The Series 2010A Bond was remarketed in June 2014 for a three-year period and in August 2017 for another three-year period that extends to August 4, 2020. The Series 2010B Bond was remarketed in August 2016 for another five-year interest period that extends to August 25, 2021.

During 2012, OVEC issued $200 million fixed-rate tax-exempt midwestern disaster relief revenue bonds (2012A Bonds) and two series of $50 million variable-rate tax-exempt midwestern disaster relief revenue bonds (2012B and 2012C Bonds). The 2012A, 2012B, and 2012C Bonds will begin amortizing on June 1, 2027, to their respective maturity dates. The variable rates listed above reflect the interest rate in effect at December 31, 2017.

In 2017, the 2012B and 2012C Bonds, which were secured by irrevocable transferable direct-pay letters of credit, expiring June 28, 2017, and June 28, 2018, were remarketed with four-year and five-year interest periods expiring August 4, 2021 and August 4, 2022, respectively.

During 2017, OVEC issued $100 million 2017A variable-rate non-amortizing unsecured senior notes (2017A Notes) to refinance and retire a 2013 series of notes (2013A). The 2013A Notes had an original maturity date of February 15, 2018. The 2017A Notes have annual repayment of $33,333,333 on August 4, 2020, August 4, 2021, and at the maturity date of August 4, 2022.

The annual maturities of long-term debt as of December 31, 2017, are as follows:

2018	$ 76,483,805
2019	154,670,115
2020	141,387,803
2021	244,982,570
2022	148,800,891
2023–2040	589,977,994
Total	$ 1,356,303,178

Note that the 2017 current maturities of long-term debt include $25 million of remarketable variable-rate bonds. The Companies expect cash maturities of as little as $51,483,805 to the extent the remarketing agents are successful in their ongoing efforts to remarket the bonds through the contractual maturity dates in February 2026 and to the extent that OVEC elects not to repurchase the bonds.

7. INCOME TAXES

OVEC and IKEC file a consolidated federal income tax return. The effective tax rate varied from the statutory federal income tax rate due to differences between the book and tax treatment of various transactions as follows:

	2017	2016
Income tax expense at 35% statutory rate	$ 537,876	$ 449,361
Temporary differences flowed through to customer bills	(546,716)	(115,669)
Permanent differences and other	8,840	11,728
Income tax provision	$ -	$ 345,420

Components of the income tax provision were as follows:

	2017	2016
Current income tax expense—federal	$ -	$ 345,420
Current income tax (benefit)/expense—state	-	-
Deferred income tax expense/(benefit)—federal	-	-
Total income tax provision	$ -	$ 345,420

OVEC and IKEC record deferred tax assets and liabilities based on differences between book and tax basis of assets and liabilities measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. Deferred tax assets and liabilities are adjusted for changes in tax rates.

On December 22, 2017, the United States Government enacted comprehensive tax legislation commonly **referred to as the Tax Cuts and Jobs Act ("TCJA"). The TCJA makes broad and complex changes to the Internal Revenue Code ("IRC"), many of which are effective on January 1, 2018, including, but not** limited to, (1) reducing the federal corporate income tax rate from 35 percent to 21 percent, (2) eliminating the use of bonus depreciation for regulated utilities, while permitting full expensing of qualified property for non-regulated entities, (3) eliminating the domestic production activities deduction previously allowable under Section 199 of the IRC, (4) creating a new limitation on the deductibility of interest expense for non-regulated businesses, (5) eliminating the corporate alternative minimum tax **("AMT") and changing how existing AMT credits can be** realized, and (6) restricting the deductibility of entertainment and lobbying-related expenses.

As a result of the reduction in the federal tax rate, the Companies recorded a revaluation adjustment to decrease deferred tax assets by $15.3 million, with a corresponding decrease of $15.3 million in the valuation allowance.

At December 31, 2017, the Companies have alternative minimum tax credit carryforwards which do not expire. Pursuant to the TCJA, the Companies now have a noncontingent right to recover their alternative minimum tax carryforwards through 2021. Accordingly, the Companies recorded $9.3 million as income taxes receivable in the accompanying balance sheets as of December 31, 2017.

To the extent that the Companies have not reflected credits in customer billings for deferred tax assets, they have recorded a regulatory liability representing income taxes refundable to customers under the applicable agreements among the parties. The regulatory liability was $11,571,428 and $5,433,716 at December 31, 2017 and 2016, respectively.

Deferred income tax assets (liabilities) at December 31, 2017 and 2016, consisted of the following:

	2017	2016
Deferred tax assets:		
Deferred revenue—advances for construction	$ 30,515	$ 3,404,026
AMT credit carryforwards	-	8,837,712
Federal net operating loss carryforwards	56,314,469	104,723,266
Postretirement benefit obligation	3,613,382	13,683,150
Pension liability	7,113,085	11,721,810
Postemployment benefit obligation	812,324	1,535,562
Asset retirement obligations	12,012,740	11,569,073
Advanced collection of interest and debt service	6,674,331	660,766
Miscellaneous accruals	1,284,013	2,158,746
Regulatory liability—other	-	-
Regulatory liability—asset retirement costs	-	4,729,118
Regulatory liability—postretirement benefits	11,870,952	9,670,762
Regulatory liability—income taxes refundable	-	-
to customers	7,302,379	15,096,997
Total deferred tax assets	107,028,190	187,790,988
Deferred tax liabilities:		
Prepaid expenses	(360,396)	(602,424)
Electric plant	(77,669,885)	(128,994,396)
Unrealized gain/loss on marketable securities	(3,649,108)	(3,694,091)
Regulatory asset—pension benefits	(7,826,970)	(12,998,618)
Regulatory asset —asset retirement costs	(142,494)	
Regulatory asset—unrecognized postemployment benefits	(812,324)	(1,535,562)
Total deferred tax liabilities	(90,461,177)	(147,825,091)
Valuation allowance	(16,567,013)	(37,265,897)
Deferred income tax assets	$ -	$ 2,700,000

As discussed in Note 1, OVEC indefinitely changed its billing practices in 2014 to effectively suspend billings for its authorized equity return. As a result, the Companies' long-term expectation is that taxable income will be breakeven for the foreseeable future. Accordingly, the Companies have recorded a valuation allowance for their deferred tax assets as of December 31, 2017 and 2016.

The accounting guidance for Income Taxes addresses the determination of whether the tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under this guidance, the Companies may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The Companies have not identified any uncertain tax positions as of December 31, 2017 and 2016, and accordingly, no liabilities for uncertain tax positions have been recognized.

The Companies file income tax returns with the Internal Revenue Service and the states of Ohio, Indiana, and the Commonwealth of Kentucky. The Companies are no longer subject to federal tax examinations for tax years 2013 and earlier. The Companies are no longer subject to State of Indiana tax examinations for tax years 2013 and earlier. The Companies are no longer subject to Ohio and the Commonwealth of Kentucky examinations for tax years 2012 and earlier. The Companies have $268,164,138 of Federal Net Operating Loss carryovers that begin to expire in 2032.

8. PENSION PLAN AND OTHER POSTRETIREMENT AND POSTEMPLOYMENT BENEFITS

The Companies have a noncontributory qualified defined benefit pension plan (the Pension Plan) covering substantially all of their employees hired prior to January 1, 2015. The benefits are based on years of service and each employee's highest consecutive 36-month compensation period. Employees are vested in the Pension Plan after five years of service with the Companies.

Funding for the Pension Plan is based on actuarially determined contributions, the maximum of which is generally the amount deductible for income tax purposes and the minimum being that required by the Employee Retirement Income Security Act of 1974, as amended.

In addition to the Pension Plan, the Companies provide certain health care and life insurance benefits (Other Postretirement Benefits) for retired employees. Substantially, all of the Companies' employees hired prior to January 1, 2015, become eligible for these benefits if they reach retirement age while working for the Companies. These and similar benefits for active employees are provided through employer funding and insurance policies. In December 2004, the Companies established VEBA trusts. In January 2011, the Companies established an Internal Revenue Code Section 401(h) account under the Pension Plan.

The full cost of the pension benefits and other postretirement benefits has been allocated to OVEC and IKEC in the accompanying consolidating financial statements. The allocated amounts represent approximately a 57% and 43% split between OVEC and IKEC, respectively, as of December 31, 2017, and approximately a 56% and 44% split between OVEC and IKEC, respectively, as of December 31, 2016.

The Pension Plan's assets as of December 31, 2017, consist of investments in equity and debt securities. All of the trust funds' investments for the pension and postemployment benefit plans are diversified and managed in compliance with all laws and regulations. Management regularly reviews the actual asset allocation and periodically rebalances the investments to targeted allocation when appropriate. The investments are reported at fair value under the Fair Value Measurements and Disclosures accounting guidance.

All benefit plan assets are invested in accordance with each plan's investment policy. The investment policy outlines the investment objectives, strategies, and target asset allocations by plan. Benefit plan assets are reviewed on a formal basis each quarter by the OVEC-IKEC Qualified Plan Trust Committee.

The investment philosophies for the benefit plans support the allocation of assets to minimize risks and optimize net returns.

Investment strategies include:

- Maintaining a long-term investment horizon.
- Diversifying assets to help control volatility of returns at acceptable levels.
- Managing fees, transaction costs, and tax liabilities to maximize investment earnings.
- Using active management of investments where appropriate risk/return opportunities exist.
- Keeping portfolio structure style neutral to limit volatility compared to applicable benchmarks.

The target asset allocation for each portfolio is as follows:

Pension Plan Assets	**Target**
Domestic equity	15 %
International and global equity	15 %
Fixed income	70 %

VEBA Plan Assets	**Target**
Domestic equity	20 %
International and global equity	20 %
Fixed income	57 %
Cash	3 %

Each benefit plan contains various investment limitations. These limitations are described in the investment policy statement and detailed in customized investment guidelines. These investment guidelines require appropriate portfolio diversification and define security concentration limits. Each investment manager's portfolio is compared to an appropriate diversified benchmark index.

Equity investment limitations:

- No security in excess of 5% of all equities.
- Cash equivalents must be less than 10% of each investment manager's equity portfolio.
- Individual securities must be less than 15% of each manager's equity portfolio.
- No investment in excess of 5% of an outstanding class of any company.
- No securities may be bought or sold on margin or other use of leverage.

Fixed-Income Limitations—As of December 31, 2017, the Pension Plan fixed-income allocation consists of managed accounts composed of U.S. Government, corporate, and municipal obligations. The VEBA benefit plans' fixed-income allocation is composed of a variety of fixed-income securities and mutual funds. Investment limitations for these fixed-income funds are defined by manager prospectus.

Cash Limitations—Cash and cash equivalents are held in each trust to provide liquidity and meet short-term cash needs. Cash equivalent funds are used to provide diversification and preserve principal. The underlying holdings in the cash funds are investment grade money market instruments, including money market mutual funds, certificates of deposit, treasury bills, and other types of investment-grade short-term debt securities. The cash funds are valued each business day and provide daily liquidity.

Projected Pension Plan and Other Postretirement Benefits obligations and funded status as of December 31, 2017 and 2016, are as follows:

	Pension Plan		Other Postretirement Benefits	
	2017	2016	2017	2016
Change in projected benefit obligation:				
Projected benefit obligation—beginning of year	$ 232,998,159	$ 210,230,403	$ 174,338,482	$ 159,175,000
Service cost	6,511,513	6,100,517	5,100,383	4,668,640
Interest cost	9,796,123	10,010,361	7,434,498	7,490,213
Plan participants' contributions	-	-	1,357,889	1,242,428
Benefits paid	(11,928,458)	(8,968,048)	(6,175,593)	(5,477,750)
Net actuarial loss (gain)	18,676,940	15,674,831	(4,131,790)	7,239,951
Plan amendments (1)	-	-	(9,436,660)	-
Expenses paid from assets	(34,854)	(49,905)	-	-
Projected benefit obligation—end of year	256,019,423	232,998,159	168,487,209	174,338,482
Change in fair value of plan assets:				
Fair value of plan assets—beginning of year	195,870,007	182,340,523	135,120,392	126,939,255
Actual return on plan assets	28,862,881	16,380,770	16,259,397	7,972,778
Expenses paid from assets	(34,854)	(49,905)	-	-
Employer contributions	6,000,000	6,166,667	4,728,439	4,443,681
Plan participants' contributions	-	-	1,357,889	1,242,428
Benefits paid	(11,928,458)	(8,968,048)	(6,175,593)	(5,477,750)
Fair value of plan assets—end of year	218,769,576	195,870,007	151,290,524	135,120,392
Underfunded status—end of year	$ (37,249,847)	$ (37,128,152)	$ (17,196,685)	$ (39,218,090)

(1) The $9.4 million plan amendment is the result of the removal of a cost of living adjustment for non-grandfathered employees. These employees are expected to receive benefits through a Medicare Exchange with OVEC's maximum annual subsidy to be limited to $4,000.

See Note 1 for information regarding regulatory assets related to the Pension Plan and Other Postretirement Benefits plan.

The accumulated benefit obligation for the Pension Plan was $230,114,000 and $208,284,000 at December 31, 2017 and 2016, respectively.

Components of Net Periodic Benefit Cost—The Companies record the expected cost of Other Postretirement Benefits over the service period during which such benefits are earned.

Pension expense is recognized as amounts are contributed to the Pension Plan and billed to customers. The accumulated difference between recorded pension expense and the yearly net periodic pension expense, as calculated under generally accepted accounting principles, is billable as a cost of operations under the ICPA when contributed to the pension fund. This accumulated difference has been recorded as a regulatory asset in the accompanying consolidating balance sheets.

	Pension Plan		Other Postretirement Benefits	
	2017	2016	2017	2016
Service cost	$ 6,511,513	$ 6,100,517	$ 5,100,383	$ 4,668,640
Interest cost	9,796,123	10,010,361	7,434,498	7,490,213
Expected return on plan assets	(11,658,739)	(10,904,733)	(7,275,382)	(6,719,397)
Amortization of prior service cost	(416,565)	(416,565)	(1,763,901)	(1,763,901)
Recognized actuarial loss (gain)	1,049,964	643,503		(75,802)
Total benefit cost	$ 5,282,296	$ 5,433,083	$ 3,495,598	$ 3,599,753
Pension and other postretirement benefits expense recognized in the consolidating statements of income and retained earnings and billed to Sponsoring Companies under the ICPA	$ 6,000,000	$ 6,166,667	$ -	$ -

The following table presents the classification of Pension Plan assets within the fair value hierarchy at December 31, 2017 and 2016:

	Fair Value Measurements at Reporting Date Using			
2017	Quoted Prices in Active Market for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Common stock	$ 9,089,309	$ -	$ -	$ 9,089,309
Equity mutual funds	43,799,989	-	-	43,799,989
Fixed-income securities	-	149,310,352	-	149,310,352
Cash equivalents	2,983,062	-	-	2,983,062
Subtotal Benefit Plan Assets	$ 55,872,360	$ 149,310,352	$ -	205,182,712
Investments measured at net asset value (NAV)				13,586,864
Total Benefit Plan Assets				$ 218,769,576
2016	(Level 1)	(Level 2)	(Level 3)	Total
Common stock	$ 9,056,579	$ -	$ -	$ 9,056,579
Equity mutual funds	40,257,125	-	-	40,257,125
Fixed income securities		127,711,240	-	127,711,240
Cash equivalents	6,727,436	-	-	6,727,436
Subtotal Benefit Plan Assets	$ 56,041,140	$ 127,711,240	$ -	183,752,380
Investments measured at net asset value (NAV)				12,117,627
Total Benefit Plan Assets				$ 195,870,007

The following table presents the classification of VEBA and 401(h) account assets within the fair value hierarchy at December 31, 2017 and 2016:

	Fair Value Measurements at Reporting Date Using			
2017	**Quoted Prices in Active Market for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**2017 Total**
Equity mutual funds	$ 55,419,961	$ -	$ -	$ 55,419,961
Fixed-income mutual funds	69,687,330	-	-	69,687,330
Fixed-income securities	-	19,304,908	-	19,304,908
Cash equivalents	736,826	-	-	736,826
Benefit Plan Assets	$ 125,844,117	$ 19,304,908	$ -	145,149,025
Uncleared cash disbursements from benefits paid				(1,839,265)
Investments measured at net asset value (NAV)				7,980,764
Total Benefit Plan Assets				$ 151,290,524
2016				
Equity mutual funds	$ 68,645,763	$ -	$ -	$ 68,645,763
Fixed-income mutual funds	41,750,065	-	-	41,750,065
Fixed-income securities	-	18,611,238	-	18,611,238
Cash equivalents	728,483	-	-	728,483
Benefit Plan Assets	$ 111,124,311	$ 18,611,238	$ -	129,735,549
Uncleared cash disbursements from benefits paid				(1,601,641)
Investments measured at net asset value (NAV)				6,986,484
Total Benefit Plan Assets				$ 135,120,392

Investments that were measured at net asset value (NAV) per share (or its equivalent) as a practical expedient have not been classified in the fair value hierarchy. These investments represent holdings in a single private investment fund that are redeemable at the election of the holder upon no more than 30 days' notice. The values reported above are based on information provided by the fund manager.

Pension Plan and Other Postretirement Benefit Assumptions—Actuarial assumptions used to determine benefit obligations at December 31, 2017 and 2016, were as follows:

	Pension Plan		Other Postretirement Benefits			
	2017	2016	2017		2016	
			Medical	Life	Medical	Life
Discount rate	3.75 %	4.31 %	3.76 %	3.76 %	4.31 %	4.31 %
Rate of compensation increase	3.00	3.00	N/A	3.00	N/A	3.00

Actuarial assumptions used to determine net periodic benefit cost for the years ended December 31, 2017 and 2016, were as follows:

	Pension Plan		Other Postretirement Benefits			
	2017	2016	2017		2016	
			Medical	Life	Medical	Life
Discount rate	4.31 %	4.82 %	4.31 %	4.31 %	4.80 %	4.80 %
Expected long-term return on plan assets	6.00	6.00	5.29	6.00	5.29	6.00
Rate of compensation increase	3.00	3.00	N/A	3.00	N/A	3.00

In selecting the expected long-term rate of return on assets, the Companies considered the average rate of earnings expected on the funds invested to provide for plan benefits. This included considering the Pension Plan and VEBA trusts' asset allocation and the expected returns likely to be earned over the life of the Pension Plan and the VEBAs.

Assumed health care cost trend rates at December 31, 2017 and 2016, were as follows:

	2017	2016
Health care trend rate assumed for next year—participants under 65	7.30 %	7.00 %
Health care trend rate assumed for next year—participants over 65	7.00	7.00
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)—participants under 65	5.00	5.00
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)—participants over 65	5.00	5.00
Year that the rate reaches the ultimate trend rate	2022	2022

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on total service and interest cost	$ 2,438,218	$ (1,883,985)
Effect on postretirement benefit obligation	25,619,686	(20,533,984)

Pension Plan and Other Postretirement Benefit Assets—The asset allocation for the Pension Plan and VEBA trusts at December 31, 2017 and 2016, by asset category was as follows:

	Pension Plan		VEBA Trusts	
	2017	2016	2017	2016
Asset category:				
Equity securities	30 %	31 %	41 %	40 %
Debt securities	70	69	59	60

Pension Plan and Other Postretirement Benefit Contributions—The Companies expect to contribute $6,000,000 to their Pension Plan and $5,000,000 to their Other Postretirement Benefits plan in 2018.

Estimated Future Benefit Payments—The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

Years Ending December 31	Pension Plan	Other Postretirement Benefits
2018	$ 8,716,563	$ 6,578,426
2019	9,496,969	7,068,992
2020	10,253,026	7,543,046
2021	11,102,802	7,938,311
2022	11,750,758	8,497,990
Five years thereafter	69,890,983	50,073,420

Postemployment Benefits—The Companies follow the accounting guidance in FASB ASC 712, *Compensation—Non-Retirement Postemployment Benefits*, and accrue the estimated cost of benefits provided to former or inactive employees after employment but before retirement. Such benefits include, but are not limited to, salary continuations, supplemental unemployment, severance, disability (including workers' compensation), job training, counseling, and continuation of benefits, such as health care and life insurance coverage. The cost of such benefits and related obligations has been allocated to OVEC and IKEC in the accompanying consolidating financial statements. The allocated amounts represent approximately a 66% and 34% split between OVEC and IKEC, respectively, as of December 31, 2017, and approximately a 59% and 41% split between OVEC and IKEC, respectively, as of December 31, 2016. The liability is offset with a corresponding regulatory asset and represents unrecognized postemployment benefits billable in the future to customers. The accrued cost of such benefits was $3,865,985 and $4,273,362 at December 31, 2017 and 2016, respectively.

Defined Contribution Plan—The Companies have a trustee-defined contribution supplemental pension and savings plan that includes 401(k) features and is available to employees who have met eligibility requirements. The Companies' contributions to the savings plan equal 100% of the first 1% and 50% of the next 5% of employee-participants' pay contributed. In addition, the Companies provide contributions to eligible employees, hired on or after January 1, 2015, of 3% to 5% of pay based on age and service. Benefits to participating employees are based solely upon amounts contributed to the participants' accounts and investment earnings. By its nature, the plan is fully funded at all times. The employer contributions for 2017 and 2016 were $1,997,840 and $1,985,582, respectively.

9. ENVIRONMENTAL MATTERS

Air Regulations

On March 10, 2005, the United States Environmental Protection Agency (the U.S. EPA) issued the Clean Air Interstate Rule (CAIR) that required significant reductions of SO_2 and NO_x emissions from coal-burning power plants. On March 15, 2005, the U.S. EPA also issued the Clean Air Mercury Rule (CAMR) that required significant mercury emission reductions for coal-burning power plants. The CAIR and CAMR emission reductions were respectively required in two phases: 2009 and 2015 for NO_x; 2010 and 2015 for SO_2; and 2010 and 2018 for mercury. Ohio and Indiana subsequently finalized their respective versions of CAIR and CAMR. In response, the Companies determined that it would be necessary to install flue gas desulfurization (FGD) systems at both plants to comply with these rules. Following completion of the necessary engineering and permitting, construction was started on the FGD systems, and the two Kyger Creek FGD systems were placed into service in 2011 and 2012, while the two Clifty Creek FGD systems were placed into service in 2013.

After the promulgation of CAIR and CAMR, a series of legal challenges to those rules resulted in their replacement with additional rules. CAMR was replaced with a rule referred to as the Mercury and Air Toxics Standards (MATS) rule. The rule became final on April 16, 2012, and the Companies had to demonstrate compliance with MATS emission limits on April 16, 2015. The MATS rule has also undergone legal challenges since it went into effect, and there are a few remaining legal issues pending. The controls the Companies have installed have proven to be adequate to meet the stringent emissions requirements outlined in the MATS rule.

After CAIR was promulgated, legal challenges resulted in that rule being remanded back to the U.S. EPA. The U.S. EPA subsequently promulgated a replacement rule to CAIR called the Cross-State Air Pollution Rule (CSAPR). CSAPR was issued on July 6, 2011, and it was scheduled to go into effect on January 1, 2012. However, a legal challenge of that rule resulted in a stay. The stay was lifted by the D.C. Circuit Court in 2014 and CSAPR, which requires significant NO_x and SO_2 emissions reductions, became effective on January 1, 2015. Further legal challenges of CSAPR resulted in the U.S. Supreme Court remanding portions of the CSAPR rule back to the D.C. Circuit Court for additional review and subsequent action by the U.S. EPA. This resulted in U.S. EPA issuing the CSAPR Update rule which became final on September 7, 2016, and went into effect beginning with the May 1, 2017 to September 30, 2017 ozone season. The CSPAR Update did not replace CSPAR, it only required additional reductions in NO_x emissions from utilities in certain states during the ozone season. The Companies prepared for and implemented a successful compliance strategy for the CSAPR Update rule requirements in the 2017 ozone season. The Companies expect that this compliance strategy will be successful for the 2018 ozone season as well.

As a result of the installation and effective operation of the FGD systems and the SCR systems at each plant, management did not need to purchase additional SO_2 allowances in 2017 to cover actual emissions. The Companies also did not need to consume additional NO_x ozone season allowances purchased strategically in advance of the 2017 ozone season as a safeguard to cover NO_x emissions in 2017 and beyond. Depending on a variety of operational and economic factors, management may elect to consume banked allowances and/or strategically purchase additional CSAPR annual and ozone season NO_x allowances in 2018 and beyond for compliance with the CSAPR Update rule.

With all FGD systems fully operational, the Companies continue to expect to have adequate SO_2 allowances available without having to rely on market purchases to comply with the CSAPR rules in their current form. Given the success of our NO_x ozone season compliance strategy in 2017, the purchase of additional NO_x allowances is less likely in the short term as well; however, we did implement changes in unit dispatch criteria for Clifty Creek Unit 6 during the 2017 ozone season and are continuing to evaluate the need for additional NO_x controls for this unit to provide additional flexibility in operating this unit under the CSAPR Update regulations as well as any future NO_x regulations.

CCR Rule

In 2010, the U.S. EPA published a proposed rule to regulate the disposal and beneficial reuse of coal combustion residuals (CCRs), including fly ash and boiler slag generated at coal-fired electric generating units as well as FGD gypsum generated at some coal-fired plants. The proposed rule contained two alternative proposals. One proposal would impose federal hazardous waste disposal and management standards on these materials and another would allow states to retain primary authority to regulate the beneficial reuse and disposal of these materials under state solid waste management standards, including minimum federal standards for disposal and management. Both proposals would impose stringent requirements for the construction of new coal ash landfills and existing unlined surface impoundments.

Various environmental organizations and industry groups filed a petition seeking to establish deadlines for a final rule. To comply with a court-ordered deadline, the U.S. EPA issued a prepublication copy of its final rule in December 2014. The rule was published in the Federal Register in April 2015 and became effective in October 2015.

In the final rule, the U.S. EPA elected to regulate CCR as a nonhazardous solid waste and issued new minimum federal solid waste management standards. The rule applies to new and existing active CCR landfills and CCR surface impoundments at operating electric utility or independent power production facilities. The rule imposes new and additional construction and operating obligations, including location restrictions, liner criteria, structural integrity requirements for impoundments, operating criteria, and additional groundwater monitoring requirements. The rule is self-implementing and currently does not require state action. As a result of this self-implementing feature, the rule contains extensive recordkeeping, notice, and Internet posting requirements.

The Companies have been systematically implementing applicable provisions of the CCR rule. The Companies have completed all compliance obligations associated with the rule to date and are continuing to evaluate what, if any, impacts groundwater quality will have on its CCR units. Preliminary background results indicate that there is a potential for groundwater quality issues with the boiler slag ponds at each plant and both landfills. This information is still being collected and evaluated, so no final determination has been made to date. Alternative source demonstrations (ASD) are already being completed in parallel to the additional groundwater evaluations. The Companies are confident in being able to demonstrate that an ASD is the cause of the preliminary groundwater quality issues being observed in the Kyger Creek landfill and boiler slag ponds.

In February 2014, the U.S. EPA completed a risk evaluation of the beneficial uses of coal fly ash in concrete and FGD gypsum in wallboard and concluded that the U.S. EPA supports these beneficial uses. Currently, approximately eight percent of the coal ash and other residual products from our generating facilities are reused in the production of cement and wallboard, as soil amendments, as abrasives or road treatment materials, and for other beneficial uses.

NAAQS Compliance for SO_2

On June 22, 2010, the U.S. EPA revised the Clean Air Act by developing and publishing a new one-hour SO_2 NAAQS of 75 parts per billion, which replaced the previously existing 24-hour and annual standards, and became effective on August 23, 2010. States with areas failing to meet the new standard are required to develop SIPs to expeditiously attain and maintain the standard.

On August 15, 2013, the U.S. EPA published its initial non-attainment area designations for the new one-hour SO_2, which did not include the areas around Kyger Creek or Clifty Creek. However, the amended rule does establish that at a minimum sources that emit 2,000 tons SO_2 or more per year be characterized by their respective states using either modeling of actual source emissions or through appropriately sited ambient air quality monitors.

In addition, U.S. EPA entered into a settle agreement with Sierra Club/NRDC in the U.S. District Court for the Northern District of California requiring U.S. EPA to take certain actions, including completing area designation by July 2, 2016, for areas with either monitored violations based on 2013-15 air quality monitoring or sources not announced for retirement that emitted more than 16,000 tons SO_2 or more than 2,600 tons with a 0.45 SO_2/mmBtu emission rate in 2012.

Both Kyger Creek and Clifty Creek either directly or indirectly triggered one of the criteria and have been evaluated by our respective state regulatory agencies through modeling. The modeling results showed Clifty Creek could meet the new one-hour SO_2 limit using their current scrubber systems without any additional investment or modifications. **Kyger Creek's modeling data was rejected by U.S.** EPA as inconclusive. As a result, Kyger Creek installed a SO_2 monitoring network around the plant and is being required to monitor ambient air quality for at least a three-year window which began on January 1, 2017. U.S. EPA will then use the results of the monitoring network data to make a determination of our compliance status with the SO_2 NAAQS by no later than December 31, 2020. Based on the first year of data from that network, OVEC expects to show compliance with the new one-hour standard, and we expect to avoid additional scrubber investments or modifications.

Steam Electric ELGs

On September 30, 2015, the U.S. EPA signed a new final rule governing Effluent Limitations Guidelines (ELGs) for the wastewater discharges from steam electric power generating plants. The rule, which was formally published in the Federal Register on November 3, 2015, was going to impact future wastewater discharges from both the Kyger Creek and Clifty Creek Stations.

The rule was intended to require the Companies to modify the way we handle a number of wastewater processes at both power plants. Specifically, the new ELG standards were going to affect the following wastewater processes in three ways listed below; however, in April of 2017, EPA issued an administrative stay on the ELG rule, and then in June of 2017, the EPA issued a separate rulemaking staying the compliance deadlines for portions of the ELG rule applicable to bottom ash sluice water and to FGD wastewater discharges. EPA intends to reeval**uate what constitutes "best available technology"** for these two wastewater discharges and issue an updated rule by no later than the fall of 2020. The original impacts and updated impacts to each wastewater discharge are highlighted below:

1. Kyger Creek will need to convert to dry fly ash handling by no later than December 31, 2023. The EPA stay on portions of the ELG rule do not impact the need to convert Kyger Creek Station to dry fly ash handling or the associated timeline. The Clifty Creek Station already has a dry fly ash handling system in place, so this provision of the rule will not impact Clifty Creek's operations.

2. The new ELG rules originally prohibited the discharge of bottom ash sluice water from boiler slag/bottom ash wastewater treatment systems. For Clifty Creek and Kyger Creek, this would have most likely resulted in conversion of each plant's boiler slag ponds to either a closed-loop sluicing system or a dry handling system for boiler slag. The Companies conducted a Phase I engineering study in 2016 to determine options and costs associated with retrofitting the plants' boiler slag treatment systems. The study results are now on hold while we await further regulatory action from EPA that will determine if these options are still appropriate or if other technology-based options will be available to demonstrate compliance. Until the new rulemaking is published associated with the ELG stay that would either change the scope or timeline for compliance, we are still expected to complete engineering, design, construction, installation, and successful operation of all controls needed to demonstrate compliance with ELGs on these discharges by no later than December 31, 2023.

3. The new ELG rules originally established new internal limitations for the FGD system wastewater discharges. Specifically, there was to be new internal limits for arsenic, mercury, selenium, and nitrate/nitrite nitrogen from the FGD chlorides purge stream wastewater treatment plant at each plant. For both Clifty Creek and Kyger Creek Stations, we were expecting to be able to meet the mercury and arsenic limitations with the current wastewater treatment technology; however, we were expecting to add some form of biological (or equivalent nonbiological) treatment system on the back end of each station's existing FGD wastewater treatment plant to

meet the new nitrate/nitrite nitrogen and selenium limitations. Installation of new controls for selenium and nitrate-nitrite nitrogen are now on hold while the Companies await further regulatory action from EPA that will determine if the biological controls are still appropriate or if other technology based options will be available to demonstrate compliance. Until the new rulemaking is published associated with the ELG stay that would either change the scope or timeline for compliance, we are still expected to complete engineering, design, construction, installation, and successful operation of all controls needed to demonstrate compliance with ELGs on these discharges by no later than December 31, 2023.

Any new ELG limits will be implemented through each station's wastewater discharge permit which is typically renewed on a five-year basis. The final compliance dates are expected to be facility-specific and negotiated with our state permit agencies based on the time needed to plan, secure funding, design, procure, and install necessary control technologies once the new rulemaking has been completed. The Companies will continue to monitor EPA regulatory actions on this rule and will respond as necessary.

316(b) Compliance

The 316(b) rule was published as a final rule in the Federal Register on August 15, 2014, and impacts facilities that use cooling water intake structures designed to withdraw at least two million gallons per day from waters of the U.S. and who also have an NPDES permit. The rule requires such facilities to choose one of seven options specified by the rule to reduce impingement to fish and other aquatic organisms. Additionally, facilities that withdraw 125 million gallons or more per day must conduct entrainment studies to assist state permitting authorities in determining what site-specific controls are required to reduce the number of aquatic organisms entrained by each respective cooling water system.

The Companies have completed the required two-year fish entrainment studies. Additional analysis is being performed in compliance with the rule, and comprehensive reports are being developed for submittal to each plant's respective state agency for review.

Currently, the Companies expect to provide the results of the comprehensive 316(b) studies and our control technology recommendations to our state regulatory agencies in 2018. The timeline for when the Companies will be required to retrofit the cooling water systems at Clifty Creek and Kyger Creek, as well as the type of retrofit required, will then be negotiated with each state regulatory agency.

10. FAIR VALUE MEASUREMENTS

The accounting guidance for Financial Instruments requires disclosure of the fair value of certain financial instruments. The estimates of fair value under this guidance require the application of broad assumptions and estimates. Accordingly, any actual exchange of such financial instruments could occur at values significantly different from the amounts disclosed.

OVEC utilizes its trustee's external pricing service in its estimate of the fair value of the underlying investments held in the benefit plan trusts and investment portfolios. The Companies' management reviews and validates the prices utilized by the trustee to determine fair value. Equities and fixed-income securities are classified as Level 1 holdings if they are actively traded on exchanges. In addition, mutual funds are classified as Level 1 holdings because they are actively traded at quoted market prices. Certain fixed-income securities do not trade on an exchange and do not have an official closing price. Pricing vendors calculate bond valuations using financial models and matrices. Fixed-income securities are typically classified as Level 2 holdings because their valuation inputs are based on observable market data. Observable inputs used for valuing fixed-income securities are benchmark yields, reported trades, broker/dealer quotes, issuer spreads, bids, offers, and economic events. Other securities with model-derived valuation inputs that are observable are also classified as Level 2 investments. Investments with unobservable valuation inputs are classified as Level 3 investments.

As of December 31, 2017 and 2016, the Companies held certain assets that are required to be measured at fair value on a recurring basis. These consist of investments recorded within long-term investments. The investments consist of money market mutual funds, equity mutual funds, and fixed-income municipal securities. Changes in the observed trading prices and liquidity of money market funds are monitored as additional support for determining fair value, and unrealized gains and losses are recorded in earnings.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Companies believe their valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

As cash and cash equivalents, current receivables, current payables, and line of credit borrowings are all short-term in nature, their carrying amounts approximate fair value.

Long-Term Investments—Assets measured at fair value on a recurring basis at December 31, 2017 and 2016, were as follows:

	Fair Value Measurements at Reporting Date Using		
2017	**Quoted Prices in Active Market for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Equity mutual funds	$ 49,400,226	$ -	$ -
Fixed-income mutual funds	10,246,444	-	-
Fixed-income municipal securities	-	90,140,833	-
Cash equivalents	4,486,457	-	-
Total fair value	$ 64,133,127	$ 90,140,833	$ -
2016			
Equity mutual funds	$ 28,106,968	$ -	$ -
Fixed-income municipal securities	-	87,163,674	-
Cash equivalents	3,731,735	-	-
Total fair value	$ 31,838,703	$ 87,163,674	$ -

Long-Term Debt—The fair values of the senior notes and fixed-rate bonds were estimated using discounted cash flow analyses based on current incremental borrowing rates for similar types of borrowing arrangements. These fair values are not reflected in the balance sheets.

The fair values and recorded values of the senior notes and fixed- and variable-rate bonds as of December 31, 2017 and 2016, are as follows:

	2017		2016	
	Fair Value	Recorded Value	Fair Value	Recorded Value
Total	$ 1,509,468,557	$ 1,381,303,178	$ 1,548,416,122	$ 1,429,281,688

11. LEASES

OVEC has various operating leases for the use of other property and equipment.

The amount in property under capital leases is $1,744,030 and $1,866,796 with accumulated depreciation of $908,732 and $949,520 as of December 31, 2017 and 2016, respectively.

Future minimum lease payments for capital and operating leases at December 31, 2017, are as follows:

Years Ending December 31	Operating	Capital
2018	$ 34,218	$ 292,230
2019	15,095	117,888
2020	7,512	131,671
2021	-	86,433
2022		63,898
Thereafter		215,891
Total future minimum lease payments	$ 56,825	908,011
Less estimated interest element		273,015
Estimated present value of future minimum lease payments		$ 634,996

The annual operating lease cost incurred was $36,610 and $41,198 for 2017 and 2016, respectively.

12. COMMITMENTS AND CONTINGENCIES

The Companies are party to or may be affected by various matters under litigation. Management believes that the ultimate outcome of these matters will not have a significant adverse effect on either the Companies' future results of operation or financial position.

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JIF-08

MOODY'S
INVESTORS SERVICE

Rating Action: Moody's affirms OVEC at Ba1, changes outlook to stable from negative

11 Dec 2018

Approximately $1.4 billion of debt outstanding

New York, December 11, 2018 -- Moody's Investors Service (Moody's) affirmed the senior unsecured ratings of the Ohio Valley Electric Corporation (OVEC) at Ba1 and revised the outlook to stable from negative.

RATINGS RATIONALE

"The stable outlook recognizes the steps taken by OVEC management to bridge the approximate 5% shortfall in its revenue stream caused by the bankruptcy of one of its sponsors, FirstEnergy Solutions Corp. (FES)", said Laura Schumacher, Senior Credit Officer. These steps have included the funding of a debt reserve and the retention of earnings that can be used to offset future payment shortfalls. The affirmation of OVEC's Ba1 rating also considers the otherwise strong cost recovery provisions of the long term Inter-Company Power Agreement (ICPA) from which OVEC's revenues are derived, and acknowledges the solid overall credit quality of the remainder of the sponsor group.

In March 2018, FES filed for Chapter 11 bankruptcy protection, sought to reject the ICPA, and stopped paying its approximately 5% share of OVEC's costs. In July 2018, the bankruptcy court granted FES's motion to reject the contract based on a "business judgment" rather than a "public interest" standard. OVEC is currently challenging the bankruptcy court's approval of FES' rejection of the ICPA, as well as the court's decision to bar the Federal Energy Regulatory Commission (FERC) from the process. OVEC's challenges have been accepted for review by the United States Court of appeals for the Sixth Circuit. In the meantime, OVEC has filed a rejection damages claim of approximately $540 million against FES. Any damage awards could be used to offset future FES obligations, including debt repayment.

Following rejection of the ICPA, the FES share of energy and capacity has been allocated to the other sponsors, who have been paying their share of OVEC's variable costs; however, no one has "stepped-up" for FES' share of OVEC's fixed cost obligations. We estimate FES' share of OVEC's fixed costs to be approximately $17 million per year. In sensitivity testing, taking into account FES' share of energy and capacity revenues that are being paid, we estimate the shortfall could be reduced to about $10-$13 million per year; however these revenues are currently being allocated to the non-defaulting sponsors. As such, OVEC is currently bearing the entire cost of the shortfall, illustrating the exposure created by the lack of step-up provision in the current ICPA.

The shortfall created by the FES default is relatively modest, and as the default was widely anticipated, OVEC management was able to take steps to mitigate its impact. These steps have included funding a debt reserve at a rate of about $30 million per year (current balance is about $60 million), and the retention of the return on equity portion of its rates (approximately $2.5 million per year) as a cushion. This equity cushion would be sufficient to cover future FES shortfalls in the event the current FES shortfall is covered by short-term borrowing.

To date, there have been no draws from the debt reserve, and as of September 30, 2018, OVEC had $60 million of unrestricted cash on hand. In addition to the debt reserve, OVEC's long-term investments include about $70 million received as part of a prior settlement with the Department of Energy (DOE) that could be utilized to cover future shortfalls. The DOE funds had been ear-marked as a source of funding for future postretirement benefits; however OVEC has the ability to include a postretirement benefits charge in the fixed costs billed to the sponsors. This additional liquidity provides sufficient near-term coverage for the FES shortfall, and we expect the sponsors will continue to work toward implementing longer term, credit enhancing improvements to the ICPA after there is resolution of the issues surrounding the FES bankruptcy.

Rating outlook

The stable outlook recognizes the credit quality and outlooks of OVEC's non-defaulting sponsors, and the company's actions to address the limited financial impact of the current, ongoing, FES default. The outlook assumes payment shortfalls will continue to be addressed with excess operating cash, existing reserves, or via short-term borrowing. The outlook assumes OVEC will continue to collect reserve funds at the current rate at least until it has accumulated a full year of debt service (currently about 45% funded), and that it will extend the maturity of its revolving credit facility well in advance of its current November 2019 termination date.

Factors that could lead to an upgrade

Rating upgrades are unlikely over the near-term. Longer term, credit supportive changes to the ICPA; such as an inclusion of a step-up provision to mitigate the risk of future sponsor payment shortfalls or defaults; an improvement in the overall credit profile of the sponsor group; or stronger financial metrics, including a debt service coverage ratio above 1.6x, could put upward pressure on the rating.

Factors that could lead to a downgrade

An inability or unwillingness to continue collecting reserves or excess operating funds sufficient to cover payment shortfalls, an inability to extend OVEC's revolving credit facility beyond its November 2019 termination date in the early part of 2019, further declines in the credit quality of any sponsors, or a sponsor payment default that was not covered by existing reserves or through a swift replacement of the defaulting party, could lead to a downgrade.

Outlook Actions:

..Issuer: Ohio Valley Electric Corporation

....Outlook, Changed To Stable From Negative

Affirmations:

..Issuer: Ohio Valley Electric Corporation

....Senior Unsecured Bank Credit Facility, Affirmed Ba1

....Senior Unsecured Regular Bond/Debenture, Affirmed Ba1

..Issuer: Indiana Finance Authority

....Senior Unsecured Revenue Bonds, Affirmed Ba1

..Issuer: Ohio Air Quality Development Authority

....Senior Unsecured Revenue Bonds, Affirmed Ba1

OVEC owns and operates two coal-fired generating power plants, Kyger Creek in Ohio and Clifty Creek in Indiana, that have a combined capacity of approximately 2,400 MW. OVEC is sponsored by nine investor-owned regulated electric utilities, two independent generating companies (subsidiaries of a utility holding company) and two affiliates of generation and transmission cooperatives (collectively, the sponsors). The sponsors purchase OVEC's power at wholesale, cost based, rates. The ownership structure is governed by a long-term Inter-Company Power Agreement (ICPA) expiring in 2040.

The principal methodology used in these ratings was US Municipal Joint Action Agencies published in October 2016. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

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