

October 30, 2009

BY HAND DELIVERY

The Honorable Kimberly D. Bose
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, D.C. 20426

RE:

E.ON U.S. LLC,
Docket No. ER10-____-000

Louisville Gas and Electric Company, et al.,
Docket No. EC98-2-____

Louisville Gas and Electric Company, et al.
Docket No. EC00-67-____

E.ON AG, et al.
Docket No. EC01-115-____

Dear Secretary Bose:

Pursuant to Sections 203 and 205 of the Federal Power Act (“FPA”), 16 U.S.C. §§ 824b & 824d, and Parts 33 and 35 of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission (“FERC” or the “Commission”), 18 C.F.R. Parts 33 and 35, E.ON U.S. LLC (“E.ON U.S.”, f/k/a LG&E Energy LLC), together with and on behalf of its public utility operating company subsidiaries Louisville Gas and Electric Company (“LG&E”) and Kentucky Utilities Company (“KU”) (collectively, “Applicants”), hereby tenders this filing seeking Commission approval to change Applicants’ method of: (i) complying with Order Nos. 888, 889 and 890 *et. seq.*,¹ and (ii) meeting certain conditions imposed by the Commission in the context

¹ *Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, 61 Fed. Reg. 21,540 (May 10, 1996), FERC Stats. & Regs. ¶ 31,036 (1996), *order on reh’g*, Order No. 888-A, 62 Fed. Reg. 12,274 (Mar. 14, 1997), FERC Stats. & Regs. ¶ 31,048 (1997), *order on reh’g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh’g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff’d in relevant part sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000) (*TAPS v. FERC*), *aff’d sub nom. New York v. FERC*, 535 U.S. 1 (2002); *Open Access Same-Time Information System (Formerly Real-Time Information Networks) and Standards of Conduct*, Order No. 889, 61 Fed. Reg. 21737 (May 10, 1996), FERC Stats.

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of Applicants' prior mergers and Applicants' exit from the Midwest Independent Transmission System Operator, Inc. ("Midwest ISO"). This filing is necessary because of the upcoming termination of the Independent Transmission Organization ("ITO") Agreement between LG&E/KU and Southwest Power Pool, Inc. ("SPP") (the "ITO Agreement").²

In July of 2009, SPP informed Applicants of its intention to terminate the ITO Agreement effective as of September 1, 2010. On October 26, 2009, SPP provided E.ON U.S. with a written notice of termination of the ITO Agreement. On that same date, SPP and E.ON U.S. filed a joint notice of termination of the agreement with the Commission.³ Despite diligent and timely efforts to identify a possible replacement ITO, no other entity has responded to requests for proposals to provide such services to date. As set forth in more detail below, Applicants request expedited consideration of this proposal due to the need to transfer certain functions currently being performed by SPP before the termination of the ITO Agreement.

I. STATEMENT OF ISSUES (18 C.F.R. § 385.203)

SPP has been performing the ITO functions for the Applicants under the terms and conditions approved by the Commission in connection with their exit from the Midwest ISO.⁴ Given SPP's notice to terminate the ITO Agreement, Applicants propose to reassign to themselves the ITO functions formerly delegated to the SPP. For the reasons stated herein, Applicants assert that this proposal is just and reasonable, particularly in light of the transparency enhancements to open access transmission service implemented by the Commission in Order No. 890 and other changed circumstances discussed below.

As explained in more detail below, Applicants request the Commission to find that: (i) pursuant to FPA Section 203(b), Applicants' proposal is consistent with certain Commission merger approval orders affecting Applicants;⁵ and (ii) pursuant to FPA Section 205, Applicants' proposed rates, terms and conditions necessary to implement the changes proposed are just and reasonable and should be accepted for filing. As demonstrated herein, these findings are

& Regs. ¶ 31,035 (1996), *order on reh'g*, Order No. 889-A, FERC Stats. & Regs. ¶ 31,049 (1997), *order on reh'g*, Order No. 889-B, 81 FERC ¶ 61,253 (1997); *Preventing Undue Discrimination and Preference in Transmission Service*, Order No. 890, 72 Fed. Reg. 12,266 (Mar. 15, 2007), FERC Stats. & Regs. ¶ 31,241 (2007) ("Order No. 890").

² The ITO Agreement is filed under Attachment Q of LG&E/KU's OATT.

³ *See Louisville Gas & Electric Co., et al., and LG&E Energy LLC*, Joint Notice of Southwest Power Pool, Inc. and E.ON U.S. LLC to Terminate the Independent Transmission Organization Agreement, filed on Oct. 26, 2009, in Docket Nos. ER06-20-000 and 001 EC06-4-000 and 001.

⁴ *Louisville Gas and Electric Co.*, 114 FERC ¶ 61,282, *order on reh'g*, 116 FERC ¶ 61,020 (2006) ("Midwest ISO Exit Order").

⁵ *See n. 6, infra.*

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appropriate given the significantly changed circumstances that have occurred since LG&E/KU's withdrawal from the Midwest ISO. Since LG&E/KU's withdrawal, the Commission has required significant increased transparency regarding the provision of services under open access transmission tariffs in Order No. 890.

With regard to FPA Section 203 specifically, Applicants request that the Commission make the following findings:

1. That Applicants' proposal satisfies the conditions established in the above-captioned "EC" dockets ("Merger Conditions")⁶ and the Midwest ISO Exit Order regarding vertical market power issues and independence; and
2. That Applicants' commitment to KU requirements customers not to re-pancake transmission rates, as set forth in the Midwest ISO exit settlement with such customers, after the termination of the ITO Agreement: (i) continues to satisfy the Merger Conditions; and (ii) mitigates any concerns regarding horizontal market power in the KU destination market that may have resulted from the company's prior mergers.

With regard to FPA Section 205, specifically, Applicants request that the Commission accept for filing a revised Open Access Transmission Tariff ("OATT"). The revised OATT has been modified to reassign the ITO functions to Applicants and to delete the ITO Agreement between Applicants and SPP and the Attachment P, which specified the ITO functions. (The revised OATT is attached hereto as Exhibit 1). Applicants also request that the Commission approve their proposed reassignment of ITO functions as just and reasonable, including a *pro forma* revised agreement with Tennessee Valley Authority ("TVA") attached hereto as Attachment Q to the OATT.

Given that the ITO Agreement will expire on September 1, 2010, and to ensure an effective transition of the ITO functions from SPP to Applicants, Applicants request that the Commission review this filing on an expedited basis, and issue a conditional approval of the proposed ITO replacement within 120 days of this filing. This conditional approval is necessary to provide LG&E/KU with sufficient time to hire staff, conduct training, and implement software changes. LG&E/KU must start this process by February 2010 to allow sufficient time to safely and reliably cut over to the new system by September 1, 2010. In any event, Applicants request that the Commission issue a final decision on the merits of this case by no later than the July 2010 Commission Meeting.

⁶ See *Louisville Gas & Elec. Co. and Kentucky Utilities Co.*, 82 FERC ¶ 61,308 at 62,222-23 (1998) ("LG&E/KU Merger Order"); *Louisville Gas & Elec. Co. and Powergen LLC*, 91 FERC ¶ 61,321 (2000) ("Powergen Merger Order"); *E.ON AG*, 97 FERC ¶ 61,049 at 61,283 (2001) ("E.ON Merger Order").

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II. EXECUTIVE SUMMARY

In this filing, Applicants seek authority to replace the current ITO arrangement after SPP's termination of the ITO Agreement by allowing the current ITO tariff administration functions to revert to Applicants. When Applicants filed with the Commission requesting authority to leave the Midwest ISO in 2005, Applicants agreed to contract with SPP to perform tariff administration functions as the ITO to ensure transparency and avoid the potential for undue discrimination. The ITO Agreement sets forth the terms and conditions under which SPP performs ITO administration functions on behalf of Applicants. Since that time, the Commission ordered enhanced open access requirements under Order No. 890, which greatly increased transparency in the provision of open access services to eliminate any potential for undue discrimination. Order No. 890 increased OASIS posting requirements, requirements for stakeholder involvement in transmission planning, and imposed Available Transfer Capability ("ATC")-related consistency requirements, thereby substantially improving the ability for the Commission and transmission customers to monitor all of the tariff administration functions currently performed by SPP under the OATT. As a result, it is no longer necessary to engage a separate entity to administer these functions, as explained in further detail below.

In Order No. 890, the Commission reformed the ATC calculation requirements in the OATT. More detail is now required to be included in the OATT and additional information must be posted on the OASIS.⁷ To address the lack of transparency in ATC calculations, the Commission required that each transmission provider include in its OATT specific detail regarding its ATC calculation methodology, and to post relevant data and models on each transmission provider's OASIS. Applicants' Order No. 890 compliance filings, which comply with these directives, have been accepted by the Commission.⁸ Applicants' ATC calculation, in light of the greatly enhanced posting and consistency requirements of Order No. 890, will be performed on a non-discriminatory basis and in a transparent manner which is open to the Commission and any customer to scrutinize; thereby ensuring customers the ability to maintain continued independent oversight over this aspect of transmission service.

In particular, Applicants plan on utilizing the same Open Access Technology International, Inc.'s ("OATI") webOASIS and webTag software systems currently employed by

⁷ The Commission directed changes be made to the tariff provisions regarding ATC calculation given its finding that transmission providers had too much discretion under the *pro forma* OATT in the calculation of ATC. This broad discretion resulted in a variety of ATC calculation methodologies in use then, very little transparency regarding the nature of the calculations, and very few clear rules governing their use. Order No. 890 at PP 62, 69, and 196.

⁸ See, e.g., Letter Order Re: Attachment C Compliance Filing, Docket No. OA08-76-001 (dated July 13, 2009); *E.ON U.S. LLC*, 127 FERC ¶ 61,276 (2009); Letter Order Re: Compliance Filing, Order No. 890-A Tariff Revisions, Docket No. OA08-76-000 (dated Jan. 9, 2009); *E.ON U.S. LLC*, 124 FERC ¶ 61,263 (2008); Letter Order Re: Compliance Filing, Order No. 890-B Compliance Filing, Docket No. OA08-140-000 (dated Feb. 24, 2008).

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SPP to calculate and post ATC, administer the OASIS, automate processing of Transmission Service Requests (“TSRs”), and check the validity of electronic tags against reserved transmission. Applicants believe that the utilization of these same systems will provide a seamless transition for customers. These systems have been modified to be in compliance with the more consistent and transparent requirements of Order No. 890.

Other provisions of the OATT will be administered by the Applicants under the stringent transparency requirements that are now applicable under Order No. 890. These requirements were not operative when LG&E/KU exited from the Midwest ISO. These requirements are also sufficient to address any possible vertical market power concerns the Commission may have regarding Applicants’ prior mergers. For instance, Order No. 890 now requires OASIS postings regarding denials of transmission service requests for affiliates and non-affiliates, postings of transmission studies that are late, posting of transmission study criteria, and the opening up of the transmission planning process.⁹ All of these requirements are designed to address the potential for vertically-integrated transmission owners to unduly discriminate against third-party customers in providing open access transmission services.¹⁰

As a result of Order No. 890’s changes, Applicants’ customers will enjoy increased open access transparency. This open access service will also be administered in a cost-effective manner. Finally, Applicants note that LG&E/KU no longer hold authorizations to charge market-based rates in their control area and, thus, at the current time, wholesale energy customers in the control area are paying cost-based rates for wholesale capacity and energy.¹¹

Applicants will also continue to meet the “Users Held Harmless” obligation set forth in Article V, section 2(A) of the Midwest ISO Transmission Owners Agreement, which requires a transmission owner seeking to withdraw from the Midwest ISO to hold existing customers harmless until the termination of their contracts. Applicants have incorporated a list of existing customers and transactions that will be covered by their commitment in Section 15.8 of the OATT, which was approved by the Commission in the Midwest ISO Exit Order, as amended.¹² Further, Applicants are contractually committed to continue shielding KU requirements customers from any transmission service rate *re-pancaking* that may occur between Applicants’ transmission system and the Midwest ISO pursuant to Applicants’ Midwest ISO Exit settlement agreement with the KU requirements customers, as amended (the “Midwest ISO Exit

⁹ See discussion *infra*.

¹⁰ Order No. 890 at PP 348-49, 376, 413.

¹¹ *LG&E Energy Marketing Inc.*, 122 FERC ¶ 61,175 (2008).

¹² See Midwest ISO Exit Order at P 43 *et seq.*; *E.ON U.S. LLC, et al.*, 116 FERC ¶61,019 at P 33 (2006); and Letter Order Re: Compliance Filing, Docket Nos. ER06-20-004 and ER06-20-005 (August 23, 2006).

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Settlement”).¹³ This Settlement has the effect of diluting market concentration in the KU destination market by increasing the number of sellers that can reach the KU Municipals.

TVA will continue to act as the Reliability Coordinator and develop models to calculate, and will continue to calculate, the Available Flowgate Capability (“AFC”). Applicants propose no changes to the current functions performed by TVA under the OATT.

III. REQUEST FOR CONDITIONAL APPROVAL AND EXPEDITED CONSIDERATION

Because the ITO Agreement with SPP will expire as of September 1, 2010, Applicants request that the Commission issue a full and final decision on the merits of this request on or before the July 2010 Commission Meeting. To this end, Applicants request that the Commission issue a conditional approval of the proposed ITO replacement within 120 days of this filing to allow for the operational cutover. LG&E/KU must start the process of hiring staff, conducting training, and implementing software changes by February 2010 to allow sufficient time to safely and reliably cut over to the new system by September 1, 2010.

A final order issued by the July 2010 Commission Meeting, with a preliminary approval within 120 days of this filing, is also consistent with the Commission’s regulations, which provide that the Commission will provide expedited review of applications of certain non-merger related applications.¹⁴

IV. OVERVIEW

This overview identifies the contents of this filing, including all exhibits hereto.

Section V.A hereof presents relevant background information, including a description of the Applicants, the Merger Conditions, and a history of Applicants’ participation in and exit from the Midwest ISO.

Section V.B hereof requests that the Commission accept certain rates for filing under FPA Section 205, including a revised Open Access Transmission Tariff (“OATT”) to implement replacement of the ITO arrangement with the new proposal. Section V.B also seeks Commission approval to continue implementation of Applicants’ current hold harmless requirement and

¹³ See notes 30 thru 38, *infra*.

¹⁴ 18 C.F.R. § 33.11(b). See also Order No. 669, FERC Stats. & Regs. ¶ 31,200 at PP 188, 194 (Commission will give expedited consideration to Section 203 applications that are not contested, do not involve mergers, and are consistent with Commission precedent, and will adopt a flexible notice period policy that will allow quick processing to allow reasonable business goals to be met).

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transmission rate settlement commitments, which nullify any negative impacts on existing transmission customers and KU requirements customers, respectively.

Section V.C hereof demonstrates that Applicants' replacement arrangement for the ITO provides a cost-effective alternative for satisfaction of the Merger Conditions, the Midwest ISO Exit Order, and Order No. 890.

Section V.D hereof discusses how Applicants plan to maintain the level of reliability which Applicants' customers have historically enjoyed, while complying with the transparency requirements of Order No. 890.

Applicants believe that their proposal complies with Order Nos. 888, 889, and 890. Overall, this filing demonstrates that transmission customers and the Commission will no longer need to rely upon a third party ITO to evaluate the operation of the transmission system and administration of the OATT. Given the transparency requirements of Order No. 890, customers and the Commission are able to monitor denials of transmission service, significant changes in ATC levels, timeliness of studies, and the development of transmission plans. These safeguards will prevent the exercise of vertical market power by Applicants.

It is of primary importance to Applicants that they meet the Commission's objectives for non-discriminatory, open access transmission service in a cost-effective and efficient manner for customers. Keeping rates low and maintaining reliability are Applicants' top priorities. Kentucky has some of the lowest retail electric rates in the nation.¹⁵ In order to maintain low rates, Applicants have developed the present proposal, which complies with Order Nos. 888 and 890, in a cost-effective manner.

This filing consists of this Application and the following supporting attachments:

- Exhibit 1 – Clean Version of Applicants' OATT;
- Exhibit 2 –Red-lining the OATT (which is red-lined against the current effective OATT, including compliance filings); and

¹⁵ On February 7, 2005, Kentucky Governor Ernie Fletcher issued an Executive Order directing the KPSC to examine the future needs for electricity in the Commonwealth. *See* Kentucky Public Service Commission, *Kentucky's Electric Infrastructure: Present and Future* at 9 (Aug. 22, 2005). The Governor specifically called for a plan that would promote investment in electric infrastructure, preserve the environment, and maintain Kentucky's "low-cost electric advantage" and low electric rates. *Id.* In response, the KPSC initiated a study and reported its findings in a report issued August 22, 2005. *See id.* In the report, the KPSC noted that Kentuckians pay the lowest electricity rates in the nation. *See id.* at 11, citing U.S. Department of Energy statistics for 2005 (average retail rate for electricity in Kentucky in 2005 is 4.47 cents per kilowatt-hour whereas the national average is 7.52 cents per kilowatt-hour).

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- Exhibit 3 – Service List.

V. ANALYSIS

A. BACKGROUND

1. Description of Applicants

LG&E and KU are Kentucky corporations, each primarily engaged in the generation, transmission, and distribution of electric energy in Kentucky. LG&E and KU are subsidiaries of E.ON U.S. which, in turn, is a subsidiary of E.ON AG (“E.ON”), a major multi-national energy company headquartered in Germany.

LG&E provides retail electric service to 390,000 customers in a service area covering approximately 700 square miles in Kentucky, including the metropolitan Louisville area and 16 surrounding counties. LG&E also purchases, distributes, and sells natural gas to over 318,000 customers within Kentucky. In 1998, LG&E’s parent company acquired KU, which provides regulated electric utility service to over 518,000 customers located in 77 Kentucky counties. Under the name Old Dominion Power, KU also provides retail electric service to over 30,000 retail customers located in five counties in Virginia.¹⁶ Altogether, KU’s service territory covers 6,600 noncontiguous square miles. In addition to its retail service, KU also sells wholesale electric energy requirements service to 12 municipalities in Kentucky.

Applicants’ retail rates and services in Kentucky are subject to the jurisdiction of the KPSC. In addition, KU’s retail activities in Virginia are subject to the jurisdiction of the Virginia State Corporation Commission. Applicants also hold authorizations from FERC to make wholesale sales of power at market-based rates outside of the LGE&E/KU control area.¹⁷

As discussed in greater detail below, as part of Applicants’ exit from the Midwest ISO, Applicants delegated certain tariff administration duties to SPP, serving as an ITO, and appointed TVA to serve as their Reliability Coordinator. Applicants’ transmission system is located on the southeastern edge of the Midwest ISO’s regional footprint and is bordered by

¹⁶ In addition to its retail service in Kentucky and Virginia, KU provides electric service to approximately five customers in one county in Tennessee.

¹⁷ *Louisville Gas & Elec. Co.*, 85 FERC ¶ 61,215 (1998) (accepting for filing joint market-based rate tariff of LG&E/KU, FERC Electric Tariff, Original Volume No. 2); *LG&E Operating Cos.*, Docket No. ER99-1623-000, Letter Order, Jun. 4, 1999 (accepting revised tariff – FERC Electric Tariff, Original Volume No. 3 – for LG&E/KU permitting limited sales to certain affiliates).

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TVA to the south, the PJM Interconnection (“PJM”) to the east, and Big Rivers Electric Corporation (“BREC”) to the west.¹⁸

Combined, LG&E and KU directly own and/or control approximately 7,820 MW (summer rated) of generation capacity and, in addition, hold minority interests in certain entities that own generation.¹⁹ Applicants self-generate the vast majority of electric power used to serve their retail customers, and are among the lowest-cost power producing utilities in the nation. Applicants also hold a distinguished record for providing electric service.²⁰ As utilities within and subject to the laws of Kentucky, Applicants are not authorized to offer retail customer choice but, instead, provide bundled electric service within franchised service territories.²¹

2. Merger Conditions

On October 9, 1997, LG&E and KU, along with their respective affiliates, submitted an application to this Commission under FPA Section 203 for authority to merge. LG&E and KU demonstrated, pursuant to the Commission’s Merger Policy Statement guidelines, that their merger would have no material adverse impact on competition, rates, or regulation. The Commission agreed and authorized the merger.²² In addressing the competition analysis submitted by LG&E and KU, the Commission noted that both companies were then participating in the development of the Midwest ISO and relied in part on this fact in determining that the merger would have no adverse impact on competition in the wholesale power market. Specifically, the Commission held:

¹⁸ Applicants are directly interconnected with the following entities: American Electric Power Corporation (member of PJM); Cinergy (member of Midwest ISO); Vectren (member of Midwest ISO); EKPC; BREC; Ohio Valley Electric Corporation; Electric Energy Incorporated; and TVA.

¹⁹ KU holds a 20-percent interest in Electric Energy, Inc. (“EEInc”). EEInc owns and operates a six-unit coal-fired generating facility, with a capacity of approximately 1,002 MW (summer rated), located in Joppa, Illinois, and its wholly-owned subsidiary Midwest Electric Power, Inc. (“MEPI”) owns and operates two gas turbines with a total capacity of approximately 74 MW (summer rate) also located in Joppa, Illinois (all, collectively, the “Joppa Facilities”). Output from the Joppa Facilities is under operation and control of subsidiaries of Ameren Corporation, the majority (80 percent) owner of EEInc. Neither KU nor any affiliate of KU has any rights to the output of the Joppa Facilities. E.ON AG, the ultimate parent of the E.ON U.S. Parties, holds certain ownership interest in Airtricity, Inc., the indirect parent of, among other non-jurisdictional entities, Munnsville Wind Farm, LLC (“Munnsville Wind Farm”), the owner of a 34.5 MW wind farm located in New York Independent System Operator balancing authority area.

²⁰ LG&E has been consistently awarded the distinction of being the most highly rated electric utility in the Midwest by consumers polled in an annual J.D. Power survey.

²¹ See, e.g., *Investigation into the Membership of Louisville Gas and Electric Company and Kentucky Utilities Company in the Midwest Independent Transmission System Operator, Inc.*, KPSC Case No. 2003-00266, Order issued July 17, 2003.

²² LG&E/KU Merger Order, 82 FERC at 62,214.

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In this case, LG&E and KU have joined [the Midwest ISO] and filed for approval to transfer operational control over their transmission facilities to the Midwest ISO. We find that the proposed mitigation measures and ratepayer protection mechanisms, in conjunction with LG&E's and KU's participation in the Midwest ISO, will ensure that the merger will not adversely affect competition, rates or regulation. On this basis, we will approve the merger without further investigation.²³

The Commission further acknowledged Applicants' right to seek to terminate their participation in the Midwest ISO development process, but advised that if they do so, the Commission "will evaluate that request in light of its impact on competition in the KU destination markets, use [its] authority under section 203(b) of the FPA to address any concerns, and order further procedures as appropriate."²⁴

Following the LG&E/KU merger, Applicants were involved in two subsequent mergers. However, neither of these mergers involved operational or physical changes to the pre-existing LG&E/KU system. In response to the application for merger of Applicants' parent, then LG&E Energy Corporation, with Powergen plc ("Powergen") in 2000, the Commission did not address Applicants' participation in the Midwest ISO.²⁵ In approving E.ON's indirect acquisition of Applicants in 2001, however, the Commission did consider Applicants' participation in the Midwest ISO. In that order, the Commission stated:

LG&E and KU have committed to transfer operational control of their transmission systems to the Midwest ISO and will remain members of the Midwest ISO at least until the end of 2002. Furthermore, they have committed to be members of a Commission-approved RTO thereafter. Therefore, they lack the ability to exploit their transmission assets to harm competition in wholesale electricity markets.²⁶

3. Applicants' Participation in and Exit from the Midwest ISO

Applicants were among the earliest participants in the Midwest ISO. They became involved in the initiative to create the Midwest ISO shortly after the formation of the initial agreement among six Midwest transmission owners on February 12, 1996. Applicants invested

²³ *Id.*

²⁴ *Id.* at 62,223.

²⁵ *Louisville Gas & Elec. Co.*, 91 FERC ¶ 61,321 (2000).

²⁶ E.ON Merger Order, 97 FERC at 61,283.

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substantial time and resources in the Midwest ISO formation process, which occurred over the succeeding two-year period and involved regular meetings among a wide range of participants, including large and small IOUs, municipal utilities and power agencies, and rural electric cooperatives (collectively, the “Transmission Owners” or “TOs”), as well as other stakeholder groups such as environmental advocates, IPPs, power marketers, industrial customers, state commissions and consumer advocates, and Transmission Dependent Utilities (“TDUs”). Applicants were signatories to the TO Agreement.

Applicants’ interests in joining the Midwest ISO were largely related to Order No. 888 and the Commission’s evolving policies regarding ISOs. In addition, Applicants strove to accommodate the Commission’s desire to manage more efficiently regional transmission service, as contemplated in Order No. 888 (although the Commission did not specify in that order a particular mechanism for the management of such service).

For the reasons set forth in Applicants’ filing in Docket ER06-20-000, on October 7, 2005, as amended on January 10, 2006, E.ON U.S. (then LG&E Energy LLC), on behalf of LG&E and KU, submitted under sections 203 and 205 of the Federal Power Act a proposal to withdraw LG&E’s and KU’s transmission facilities from the transmission system operated by Midwest ISO. In an order dated March 17, 2006, the Commission conditionally accepted LG&E and KU’s proposal to withdraw from Midwest ISO.²⁷

LG&E and KU withdrew from Midwest ISO effective September 1, 2006.

B. REQUESTED APPROVALS UNDER FPA SECTION 205

Applicants request that the Commission accept for filing a revised *pro forma* OATT (which has been modified as set forth herein), which is attached hereto as Exhibit 1.

1. The Reassignment of ITO Functions Back to Applicants is Just and Reasonable Given Current Enhanced Open Access Requirements Post-Order No. 890.

Applicants request that the Commission approve their proposal to reassign the ITO functions currently carried out by SPP back to Applicants in light of the Commission’s improvements in open access transmission afforded under Order No. 890. These improvements were not in place when Applicants exited the Midwest ISO and proposed the ITO arrangement. Applicants also point out that existing transmission customers will continue to be protected under Applicants’ current transmission rate settlement commitments with the KU requirements

²⁷ See Midwest ISO Exit Order PP 1-7.

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customers, as set forth in the Midwest ISO Exit Settlement, and hold harmless commitments for existing customers, as set forth in Applicants' OATT, discussed below.

Applicants received verbal notice of termination of the ITO Agreement from SPP on July 24, 2009. Applicants conducted a Request for Interest process and only one potential entity responded that it was interested in providing replacement ITO services. E.ON U.S. provided this entity with a Request for Proposal, but this entity has subsequently withdrawn its offer of interest. Therefore, despite diligent and timely efforts to identify a possible replacement ITO, currently no such option exists.

2. SPP Provided Notice of Termination of the ITO Agreement.

Section 4.4 of the ITO Agreement provides that any party (LG&E/KU or SPP) may terminate the agreement at the end of the initial term (*i.e.*, from September 1, 2006 until August 31, 2010) or any subsequent term upon 180 days prior written notice to the other party. In July of 2009, SPP informed Applicants of its intention to terminate the ITO Agreement as of August 31, 2010. SPP followed up with a written notice, as required by the ITO Agreement on October 26, 2009. SPP has provided Applicants with notice of termination of the ITO Agreement well before the notice period required therein to allow sufficient time for Applicants to transition the ITO services.

3. Applicant's Proposal Avoids Future Increased Payments to SPP for ITO Services.

The Commission should accept for filing Applicants' request to replace SPP. The replacement arrangement is reasonable because continuation of an ITO arrangement could mean higher costs for Applicants' native load customers. The ITO and LG&E/KU recently entered a settlement whereby the ITO received an additional \$2.3 million payment under the initial term of the ITO Agreement from the original \$3.4 million per year approved initially.²⁸ Applicants' proposal is an efficient and cost-effective means of fulfilling Order No. 890 objectives, because the benefits of engaging an independent tariff administrator such as SPP are small compared to the continually increasing costs of the ITO arrangement, given Applicants' existing stringent transparency requirements.

4. Transmission Customers Are Not Adversely Affected.

Applicants' proposal will not adversely impact existing transmission customers. Applicants propose to use the same formula rate for transmission service contained in

²⁸ See Settlement Agreement submitted in *Southwest Power Pool, Inc., v. Louisville Gas & Electric Co., Kentucky Utilities Co.*, Docket Nos. EC06-4-000, *et al.*; ER06-20-000, *et al.*, on October 19, 2009.

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Attachment O of the LG&E/KU OATT. Accordingly, there will be no transmission rate level impact on customers.

a. The Existing Hold Harmless Condition Set Forth in the Midwest ISO Exit Order that applied to Existing Customers referenced in the OATT Is Maintained.

In connection with their exit from the Midwest ISO, Applicants agreed that all transmission agreements, GFAs, and OASIS reservations in place as of December 28, 2004 would receive service and pricing that they would have been entitled to receive, absent Applicants' withdrawal, until termination of such agreements (collectively, "Existing Customers").²⁹ Applicants implemented this hold harmless requirement in Section 15.8 of the LG&E/KU OATT, as follows:

- "Drive-In" to the Midwest ISO: With respect to any transaction in which an Existing Customer sells electricity generated with a source in the Applicants' control area and a sink in the Midwest ISO: (i) Applicants will waive Tariff and ancillary services billings, as applicable, which otherwise would have been incurred to transmit electricity to the Midwest ISO/LG&E/KU interface; and (ii) the Existing Customer will continue to be responsible for all Midwest ISO charges incurred to deliver such electricity to any point within the Midwest ISO beyond the Midwest ISO/LG&E/KU interface;
- "Drive-Out" to the Midwest ISO: With respect to any transaction in which an Existing Customer purchases electricity from a source in the Midwest ISO for delivery to such party's load interconnected with the Applicants' Transmission System: (i) Applicants will credit their Tariff and ancillary services billings, as applicable, to the Existing Customer by an amount equal to the Midwest ISO charges which the customer incurs to deliver such purchased electricity to the Midwest ISO/LG&E/KU interface, (provided, however, that no credit will be applied for any Midwest ISO charge for service that is not provided and charged by Applicants, *i.e.*, where there would be no pancaked charge) less any revenue that the Existing Customer receives as a TO under the Midwest ISO; and (ii) the Existing Customer will continue to be responsible for the Tariff and ancillary services billings, as applicable, incurred to deliver such electricity to their loads on the Applicants' Transmission System; and

²⁹ See n. 12, *supra*.

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- For transactions that source in a Control Area other than the Midwest ISO and sink in the Applicants' Control Area, these Existing Customers will still only pay Applicants' Tariff and ancillary services charges.

Applicants propose to maintain current OATT hold harmless commitment to Existing Customers pursuant to the terms and conditions set forth therein.

b. The Existing Settlement Commitment to the KU Municipal Requirements Customers Is Maintained.

In the Midwest Exit Order, the Commission noted that the Rate De-Pancaking Maintenance Plan ("RDMP") could not be implemented without a reciprocity agreement from the Midwest ISO. The Commission allowed Applicants to choose between obtaining a reciprocity agreement with the Midwest ISO or, at least in the meantime, establishing a hold harmless mechanism for KU requirements customers.³⁰ Despite Applicants' numerous attempts, the Midwest ISO was not interested in entering into such an agreement. Because the Applicants did not have a reciprocity agreement with the Midwest ISO that would enable de-pancaking between the two transmission systems, Applicants agreed to meet their compliance obligation by implementing the Commission's suggested alternative, *i.e.*, entering into arrangements to ensure that KU requirements customers are protected.

The "KU requirements customers" referenced in the Midwest ISO Exit Order include the Cities of Barbourville, Bardstown, Bardwell, Benham, Corbin, Falmouth, Frankfort, Madisonville, Nicholasville, and Providence; and Berea College.³¹ On February 2, 2006, Applicants filed a service agreement with these customers as well as the Frankfort Electric and Water Plant Board, Owensboro Municipal Utilities, and the TVA Distributors Group.³² The service agreement, which is designated as stand-alone rate schedule No. 402, was accepted for filing on March 17, 2006.³³ In compliance with the July 7, 2006 Order,³⁴ on July 19, 2006 Applicants submitted an amended rate schedule No. 402 with the KU requirements customers.³⁵

³⁰ Midwest ISO Exit Order at PP 108-14.

³¹ *See Louisville Gas & Elec. Co.*, 82 FERC ¶ 61,308 at n.7 (1998).

³² *See Service Agreement Between LG&E, KU, the Kentucky Municipals, and TVA Distributor Group*, Filed in Docket No. ER06-602-000 on Feb. 2, 2006. The TVA Distributor Group includes: Paducah Power System, Glasgow Electric Plant Board, Princeton Electric Plant Board, Hopkinsville Electric System, and the Duck River Electric Membership Cooperative of Shelbyville, Tennessee.

³³ *Kentucky Utilities*, Letter Order, Docket No. ER06-602-000, Mar. 17, 2006.

³⁴ *E.ON U.S., LLC, et al.*, 116 FERC ¶ 61,019 (2006) ("July 7 Order").

³⁵ This revised rate schedule No. 402 is also referred to herein as the "Midwest ISO Exit Settlement."

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The amended agreement provides an explicit mechanism to shield KU requirements customers from re-pancaked transmission and ancillary services charges upon Applicants' withdrawal from Midwest ISO. Specifically, it provides a credit to KU requirements customers for pancaked transmission and ancillary services charges. This method was suggested by the Commission.³⁶ The crediting provisions of the amended agreement were effective upon Applicants' withdrawal from the Midwest ISO.³⁷ The Commission has found that the terms of this revised agreement satisfy the Commission's condition that Applicants shield the KU requirements customers from re-pancaking of rates as a result of their withdrawal from the MISO.³⁸

5. The Revised Open Access Transmission Tariff is Just and Reasonable.

Applicants hereby file a revised OATT that discontinues the ITO as a third party acting as tariff administrator for Applicants' Transmission System. This revised OATT contains revisions to the currently effective OATT. For ease of comparison, Applicants attach hereto as Exhibit 2 a red-lined version of the OATT, which shows changes made to portions of the OATT that is currently in effect (including compliance filings).

As described below, the OATT should be accepted for filing. The following is an overview and key highlights of Applicants' proposed OATT.

- The Body of the OATT - Applicants have made minor modifications to the main body of the OATT to delete references to SPP as the ITO and assign the ITO functions to themselves.
- Attachments A through- R – These attachments have been merely re-filed with changes to reflect the reassignment of responsibilities to Applicants.
- Removal of the ITO Agreement; addition of *pro forma* revised TVA agreement - Applicants deleted from the OATT the ITO Agreement and filed a *pro forma* revised bilateral agreement between Applicants and TVA to indicate the reassignment of ITO functions to Applicants.
- Removal of Attachment P – Applicants deleted Attachment P to avoid duplication, since it provides for the SPP and TVA functions, and the TVA functions are also provided in Attachment Q.

³⁶ July 7 Order at n. 33.

³⁷ Midwest ISO Exit Order at P 95; *E.ON U.S. LLC, et al.*, 116 FERC ¶61,019 (2006) at P 38; and Letter Order Re: Compliance Filing, Docket Nos. ER06-20-004 and ER06-20-005 (August 23, 2006).

³⁸ Letter Order Re: Compliance Filing, Docket Nos. ER06-20-004 and ER06-20-005 (August 23, 2006).

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- Removal of Attachment B to the Reliability Coordinator Agreement set forth in Attachment Q – Applicants deleted Attachment B because it has been superseded by Attachment K of the OATT.

6. The Former ITO Duties will be performed by Applicants subject to Functional Independence and Greatly Increased Transparency.

The following discussion highlights key elements of the ITO's responsibilities, and how those functions will be performed under Applicants' proposal. Transferring the ITO functions to the Applicants' transmission function employees will continue to meet the Commission's goals of achieving the requisite levels of independence and transparency. All transmission function employees will continue to be functionally independent as they continue to be subject to the Commission's Order No. 2004 Standards of Conduct *et al.*,³⁹ which are designed to keep all transmission function employees of vertically-integrated utilities functionally separated from their affiliated merchant generation division. Also, transmission function employees will be subject to increased transparency in providing open access transmission service through increased OASIS posting requirements and more stakeholder involvement in the transmission planning process imposed by Order No. 890.

Those changes in the requirements for providing open access transmission address any possible vertical market power concerns by substantially improving the ability for the Commission and transmission customers to monitor the performance of many of the functions that will be transferred from SPP to the Applicants, thereby ensuring that Applicants do not, and will not, unduly discriminate in favor of their affiliates. The new functionality remains consistent with the public interest, and the implementing rates should be accepted as just and reasonable.

a. Granting and Denying Transmission Service Requests

Under their proposal, Applicants will accept or reject TSRs on a non-discriminatory basis, including requests for Network Integration Transmission and Point-to-Point service, subject to the more recent stringent transparency requirements of Order No. 890. Applicants will

³⁹ *Standards of Conduct for Transmission Providers*, Order No. 2004, FERC Stats. & Regs. ¶ 31,155 (2003), *order on reh'g*, Order No. 2004-A, FERC Stats. & Regs. ¶ 31,161, *order on reh'g*, Order No. 2004-B, FERC Stats. & Regs. ¶ 31,166, *order on reh'g*, Order No. 2004-C, FERC Stats. & Regs. ¶ 31,172 (2004), *order on reh'g*, Order No. 2004-D, 110 FERC ¶ 61,320 (2005), *vacated and remanded as it applies to natural gas pipelines sub nom. National Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831 (D.C. Cir. 2006); *see Standards of Conduct for Transmission Providers*, Order No. 690, FERC Stats. & Regs. ¶ 31,237, *order on reh'g*, Order No. 690-A, FERC Stats. & Regs. ¶ 31,243 (2007); *see also Standards of Conduct for Transmission Providers*, Notice of Proposed Rulemaking, FERC Stats. & Regs. ¶ 32,611 (2007); Notice of Proposed Rulemaking, FERC Stats. & Regs. ¶ 32,630 (2008).

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be obligated to document all transmission service requests, whether the request was granted or denied, and the supporting data underlying their ultimate decision. Additionally, Applicants will be required to post information regarding denials of transmission service for affiliates and non-affiliates, as described in more detail below.

i. Performing TTC/ATC Calculations

The determination that there is ATC is an essential step in granting new Transmission Service Requests, or TSRs. Applicants propose to perform all Total Transfer Capability (“TTC”) and ATC calculations used to determine whether transmission is available in a manner consistent with the terms of the OATT, and to ensure that all TTC and ATC values are calculated on a non-discriminatory basis. As part of these functions, Applicants will calculate ATC on a control area-to-control area basis for Applicants’ control area interfaces. It is important to note, however, that TVA will continue to calculate AFC, from which the ATC is derived.

Applicants assert that allowing them to calculate ATC is appropriate in view of the changes imposed in Order No. 890, which increased transparency and consistency in the ATC calculations. Specifically, to address the lack of prior consistency in calculating ATC, in Order No. 890, the Commission required transmission providers to provide, in Attachment C, detailed descriptions for calculating both firm and non-firm ATC. With this measure, the Commission believed there would only be a few industry-wide ATC calculation formulas.⁴⁰ As required by Order No. 890, Applicants have developed a specific methodology for assessing firm and non-firm ATC on a non-discriminatory and transparent basis which is posted on the OASIS. The ATC will be calculated using a flow-based approach, described in detail in Attachment C of Applicants’ OATT. This methodology will be applied in compliance with the Joint Reliability Coordinator Agreement (“JRCA”) and its related Congestion Management Process (“CMP”) among TVA, the Midwest ISO and PJM Interconnection, LLC, which is included in Attachment Q of Applicants’ OATT.

In addition, allowing Applicants to calculate ATC is appropriate given the greatly increased transparency in the use of ATC in granting and denying open access transmission services. In this regard, Applicants must now post the detailed information, including: (1) the number of affiliate versus non-affiliate requests for service that have been rejected, and (2) the number of affiliate versus non-affiliate requests for service that have been made. This posting must detail the length of service request (*e.g.*, short-term or long-term) and the type of service requested (*e.g.*, firm point-to-point, non-firm point-to-point or network service). Applicants must also post their underlying load forecast assumptions for all ATC calculations and post, on a

⁴⁰ Order No. 890 at P 207. Also, public utilities, working through NERC and NAESB, were directed to revise reliability standard MOD-001 to require ATC to be recalculated by all transmission providers on a consistent time interval and in a manner that closely reflects the actual topology of the system, *e.g.*, generation and transmission outages, load forecast, interchange schedules, transmission reservations, facility ratings, and other necessary data.

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daily basis, their actual daily peak load for the prior day.⁴¹ Order No. 890 also requires posting of explanations for changes in ATC when ATC levels change significantly or remain at zero for an extended period, greatly increasing transparency regarding ATC availability.⁴²

ii. Performing System Impact Studies related to TSRs

In evaluating TSRs, Applicants propose that they be responsible for performing any System Impact Studies (“SIS”) required by the OATT. Allowing Applicants to perform the SIS studies is consistent with the *pro forma* tariff. In addition, Order No. 890 now imposes requirements for completing studies on a timely basis, penalties for late studies, and the reporting of statistics concerning the amount of time required for performing affiliate and non-affiliate studies.⁴³ Applicants assert that any concerns about transmission owners delaying studies in an unduly discriminatory manner are addressed by these requirements and penalties. Applicants will continue to provide the transmission customer with the Facilities Study Agreement and will continue to coordinate, oversee, and finalize the Facilities Studies.

b. Processing Generator Interconnection Requests

Applicants will now process all interconnection requests, in accordance with the LGIP/SGIP procedures. This includes: (i) implementing and applying their generator interconnection procedures in accordance with the terms in Attachments J and K; (ii) queuing all interconnection requests; (iii) performing studies necessary to evaluate the interconnection requests; and (iv) developing transmission system modeling processes, software and assumptions used to evaluate interconnection requests. Applicants will continue to be responsible for developing and filing with the Commission procedures for any Interconnection Impact Studies, and will now be performing the Interconnection Feasibility Study and Interconnection Impact Study in accordance with the LGIP/SGIP procedures adopted in Order No. 2003 *et. seq.*⁴⁴

⁴¹ *Id.* at P 413.

⁴² *Id.* at PP 369-371.

⁴³ Order No. 890 requires transmission provider to file a notice with FERC if the transmission provider processes more than 20% of non-affiliates’ studies outside of the 60-day due diligence deadlines for two consecutive quarters. Order No. 890 at P 1319. Transmission providers are subject to penalties when they fail to meet the prescribed 60-day due diligence deadlines. The transmission provider will be subject to penalties if it continues to be out of compliance with the *pro forma* OATT requirements for each of the two quarters following the notification filing. *Id.* at P 1340. A transmission provider is out of compliance if it completes 10% or more of non-affiliates’ studies outside of the 60-day period. *Id.*

⁴⁴ *Standardization of Generator Interconnection Agreements and Procedures*, Order No. 2003, FERC Stats. & Regs. ¶ 31,146 (2003), *order on reh’g*, Order No. 2003-A, FERC Stats. & Regs. ¶ 31,160, *order on reh’g*, Order No. 2003-B, FERC Stats. & Regs. ¶ 31,171 (2004), *order on reh’g*, Order No. 2003-C, FERC Stats. & Regs. ¶ 31,190 (2005), *aff’d sub nom. Nat’l Ass’n of Regulatory Util. Comm’rs v. FERC*, 475 F.3d 1277 (D.C. Cir. 2007) (“Order No. 2003-C”).

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In requiring all Transmission Providers to adopt the Commission's *pro forma* generation interconnection procedures and standard generator interconnection agreements in Order No. 2003, the Commission's goal was to ensure that all generating facilities that will make sales for resale of electric energy in interstate commerce are offered interconnection service on comparable terms. Order No. 2003's standardized procedures and agreements were designed to prevent undue discrimination, preserve the reliability of the nation's transmission system, and lower prices for customers by allowing a variety of generation resources to compete in wholesale electricity markets. They are also designed to benefit customers by establishing the just and reasonable terms and conditions for interconnecting to the transmission grid, while ensuring that reliability is protected.⁴⁵ In light of the standardized procedures and agreements adopted in Order No. 2003, which are now incorporated in the OATT, Applicants assert that it is appropriate for them to administer the processing of interconnection requests.

c. Performing Transmission System Planning with Stakeholder Input

Transmission Planning will continue to be conducted under Order No. 890's open planning process as included in Attachment K to the LG&E/KU tariff, which includes active stakeholder participation and timely opportunities for stakeholder input throughout the entire planning cycle. This stakeholder input negates the need for a third-party ITO to provide additional oversight in the planning process in light of the enhanced transparency set forth by Order No. 890 as explained herein (*see* discussion *infra* at Section V.C.3.c).

7. TVA will continue to perform the Reliability Coordinator Functions – NERC Standards and Transmission Line Loading Relief.

The Reliability Coordinator (TVA) will continue to perform all functions identified for Reliability Coordinators under NERC's Reliability Standards,⁴⁶ while Applicants will continue

⁴⁵ See, e.g., Order No. 2003-C at P 1.

⁴⁶ NERC's Operating Reliability Subcommittee specifies the NERC Reliability Standards that implicate Reliability Coordinators. These standards include: (i) TOP-001-1 ("Reliability Responsibilities and Authorities"); (ii) TOP-003-0 ("Planned Outage Coordination"); (iii) TOP-005-1.1 ("Operating Reliability Information"); (iv) TOP-006-1 ("Monitoring System Conditions"); (v) COM-001-1.1 ("Telecommunication"); (vi) COM-002-2 ("Communications and Coordination"); (vii) EOP-002-2.1 ("Capacity and Energy Emergencies"); (viii) EOP-004-1 ("Disturbance Reporting"); (ix) EOP-006-1 ("Reliability Coordination - System Restoration"); (x) EOP-008-0 ("Plans for Loss of Control Center Functionality"); (xi) CIP-001-1 ("Sabotage Reporting"); (xii) PER-004-1 ("Reliability Coordination - Staffing"); (xiii) IRO-001-1.1 ("Reliability Coordination - Responsibilities and Authorities"); (xiv) IRO-002-1 ("Reliability Coordination - Facilities"); (xv) IRO-003-2 ("Reliability Coordination - Wide Area View"); (xvi) IRO-004-1 ("Reliability Coordination - Operations Planning"); (xvii) IRO-005-2 ("Reliability Coordination - Current Day Operations"); and (xviii) IRO-006-4 ("Reliability Coordination - Transmission Loading Relief"), available at <http://www.nerc.com/page.php?cid=2|20>.

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to retain all remaining NERC obligations. Applicants do not propose to change any of the functions granted to the Reliability Coordinator in Docket ER06-20-000. In particular, Applicants point out that TVA, not Applicants, will continue to determine AFC values and flowgate allocations and implement Transmission Line Loading Relief (“TLR”).

C. REQUESTED FINDINGS UNDER FPA SECTION 203

1. Applicants’ Proposal is Consistent with their Merger Commitments.

As described above, Applicants have been a party, directly or indirectly, to three major merger transactions. Applicants obtained prior Commission approval of these transactions under FPA Section 203 through a demonstration that each transaction was “consistent with the public interest.”⁴⁷ In particular, Applicants demonstrated that each proposed transaction will have no adverse effect on competition, rates, or regulation.⁴⁸ In reaching this determination in the KU Merger and the E.ON Merger transactions, the Commission relied in part on Applicant’s Midwest ISO membership as a factor mitigating any potential competitive concerns.

2. Applicants’ Proposal Will Achieve the Same Independence Objectives in the Performance of the Functions Transferred from the ITO.

Applicants’ proposal preserves the horizontal and vertical benefits of a third-party ITO operator. The Commission has found that Applicants’ proposal to maintain current rate de-pancaking to KU requirements customers under the Midwest ISO Exit Settlement addresses the Commission’s concerns regarding horizontal market power and will also be consistent with or superior to the *pro forma* OATT.⁴⁹ The Commission has also found that, when Applicants proposed to exit the Midwest ISO and agreed to engage SPP and TVA as their ITO and Reliability Coordinator, respectively, Applicants satisfied concerns relating to transmission-related vertical market power.⁵⁰

The ITO functions currently performed by SPP are now subject to more stringent transparency requirements set forth in Order No. 890, which eliminate any room for discrimination if these functions were to be performed directly by Applicants. Specifically,

⁴⁷ 16 U.S.C. § 824b(a).

⁴⁸ *See Inquiry Concerning the Commission’s Merger Policy Under the Federal Power Act: Policy Statement*, Order No. 592, FERC Stats. & Regs. ¶ 31,044 at 30,111 (1996) (“Merger Policy Statement”), *reconsideration denied*, Order No. 592-A, 79 FERC ¶ 61,321 (1997); *Revised Filing Requirements Under Part 33 of the Commission’s Regulations*, Order No. 642, FERC Stats. & Regs. ¶ 31,111 at 31,874-78 (2000) (“Order No. 642”), *on reh’g*, Order No. 642-A, 94 FERC ¶ 61,289 (2001).

⁴⁹ Midwest ISO Exit Order at PP 108-109.

⁵⁰ *Id.* at PP 5-6.

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Applicants will perform transmission planning subject to the enhanced transparency and stakeholder participation requirements of Order No. 890 (as described in detail above). These requirements will ensure that Applicants' performance of ITO services will be provided on a transparent and non-discriminatory basis.

3. Applicants' Replacement Proposal for the ITO Will Not Adversely Affect Competition, Rates, or Regulation.

In evaluating whether a proposed jurisdictional transaction is consistent with the public interest as required by FPA Section 203, the Commission evaluates whether the proposed transaction will have an adverse effect on competition, rates, or regulation.⁵¹ Applicants demonstrate below that their replacement proposal for the ITO functions will not have an adverse effect on competition, rates, or regulation.

a. Applicants' Replacement Proposal Will Not Adversely Affect Competition in the LG&E/KU Markets.

In Order No. 642, the Commission stated that its objective in analyzing a proposed transaction's effect on competition is to determine whether such disposition "will result in higher prices or reduced output in electricity markets."⁵² The Commission has held that higher prices and reduced output in electricity markets may occur if a FPA Section 203 applicant or applicants are able to exercise market power, either alone or in coordination with other firms.⁵³ Applicants' replacement for the ITO functions will have no such adverse impact on either horizontal or vertical competition.

b. Applicants' Replacement Proposal Will Not Adversely Affect Horizontal Competition.

In the *Merger Policy Statement*, as affirmed in Order No. 642, the Commission adopted a "delivered price test" as a screen in order to measure the effect of a proposed transaction on the ability of entities to exercise market power in generation with respect to two measures of capacity – Economic Capacity and Available Economic Capacity.⁵⁴ Appendix A of the *Merger Policy Statement* details the analytic methodology that merger applicants were required to follow

⁵¹ See *supra* n. 47.

⁵² Merger Policy Statement, FERC Stats. & Regs. at 30,130-32; Order No. 642, FERC Stats. & Regs. at 31,879.

⁵³ *Id.*

⁵⁴ *Id.* at 31,871-72.

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in their applications and that the Commission used in screening the competitive impact of mergers (the “Competitive Analysis Screen”).⁵⁵

The Competitive Analysis Screen was intended for application to situations where two or more entities in the same or nearby geographic markets proposed to merger or otherwise transfer control of generating assets. It was not intended as a tool for analyzing general changes in market concentration resulting from, for example, possible changes of the entity performing ITO functions within an existing market. Thus, the Competitive Analysis Screen may be of only marginal use for analyzing the competitive effects of Applicants’ replacement proposal for the performance of the ITO functions.

As stated by the Commission in the Midwest ISO Exit Order, Applicants’ proposal not to re-pancake transmission rates for KU requirements customers “will preserve the KU requirements customers’ access to competing suppliers, and thus will preserve the expanded geographic scope of the market that resulted from Applicants’ participation in the Midwest ISO.”⁵⁶ Under the instant proposal, Applicants will maintain their commitment to KU requirements customers not to re-pancake transmission rates, as provided for in the Midwest ISO Exit Settlement (which, as discussed above, is designated as stand-alone revised rate schedule No. 402). Applicants believe this credit mechanism addresses the Commission’s concerns regarding horizontal market power. Applicants’ contractual commitment to maintain the rates for KU requirements customers set forth in the Midwest ISO Exit Settlement is also consistent with or superior to the *pro forma* OATT.⁵⁷

c. Applicants’ Proposal Will Not Adversely Affect Vertical Competition.

In Order No. 642, the Commission set forth guidelines to be used in determining whether a proposed merger transaction would have an adverse effect on vertical competition.⁵⁸ Ordinarily, such concerns arise in circumstances in which the combined entity may restrict potential downstream competitors’ access to upstream supply markets or increase potential competitors’ costs. Applicants’ proposal for reassignment of ITO functions presents no such concerns. As explained above, Applicants have on file an Order No. 890 compliant OATT that provides enhanced non-discriminatory open access to their transmission lines. This fact alone should be sufficient to alleviate any concerns that vertical competition may be adversely affected

⁵⁵ *Id.* at 30,128-37.

⁵⁶ Midwest ISO Exit Order at P 95.

⁵⁷ *See* n. 49, *supra*.

⁵⁸ Order No. 642, FERC Stats. & Regs. at 31,904-07.

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by Applicants' replacement proposal.⁵⁹ Regardless, Applicants' proposal will ensure that there will be no adverse effect on vertical competition following the allocation of ITO functions to Applicants.

In the Midwest ISO Exit Order, the Commission outlined five specific areas where an independent entity, such as an ISO, can mitigate transmission related vertical market power, each of which of is discussed below.⁶⁰

First, as to system expansion, the Commission found that an ISO could improve the process for determining system expansion needs because it would not be dominated by the Transmission Owner.⁶¹ Under the current proposal, expansion planning will be performed by the Applicants with stakeholder involvement through the enhanced transparency requirements of Order No. 890, as specified in LG&E/KU's Attachment K to the OATT.

SPP was responsible for posting on OASIS the Planning Criteria, Applicants' business practices for transmission planning, and a description of any disputes regarding the development of the Planning Criteria, Base Case Model or the Annual Plan. It is now a requirement of Order No. 890 for the Transmission Owner to post transmission planning criterion and business practices. E.ON U.S. circulated its planning criteria to its stakeholders for comment and received no adverse responses and its planning criteria are now posted. E.ON U.S. also circulated its business practices and incorporated revisions to address stakeholders' concerns. E.ON U.S. also committed to posting changes in the business practices for stakeholder review prior to implementation absent an emergency situation. Finally, as noted above, under Order No. 890's Attachment K process, stakeholders are now involved in developing the annual plan and thus, will be aware of what changes are being made to the annual plan.

The ITO also performed duties of OASIS management, including accepting and processing requests for transmission service and determining ATC and processing generation interconnection studies. Applicants note that OASIS management is now primarily automated through the OATI, available at: www.oati.com. And, as noted above, Applicants will calculate ATC under the more transparent ATC methodology now included in Attachment C of E.ON U.S.'s OATT pursuant to Order No. 890 requirements, as discussed above. Applicants are also required to post any late studies and explain why they are late, which should satisfy processing concerns.

⁵⁹ See, e.g., *IES Utilities, Inc.*, 78 FERC ¶ 61,023 at 61,095 (1997) ("Applicants' open access tariffs mitigate any transmission market power they may possess post merger."). See also Order No. 888, FERC Stats. & Regs. at 31,656-57 ("In order to demonstrate the requisite absence or mitigation of transmission market power, a transmission-owning public utility seeking to sell at market-based rates must have on file with the Commission an open access transmission tariff for the provision of comparable service.").

⁶⁰ See Midwest ISO Exit Order at PP 81-95.

⁶¹ *Id.* at P 82.

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Second, the Commission looked at whether the management of congested interfaces would be problematic and found that neither SPP nor TVA had an economic stake in congestion management issues. The Commission noted that SPP would calculate ATC and TTC, and validate interchange schedules.⁶² As noted previously, under the current proposal, Applicants will perform such functions under ATC regulations that result in more consistent calculations and posting requirements. TVA will continue to be responsible for coordination on interfaces with other control areas.

Third, the Commission considered the potential for abuses related to a Transmission Owner's priority to use internal system capacity for native load to make off-system sales.⁶³ Under Order No. 890, the Transmission Owner must post when it denies a transmission service request and provide information regarding denials of transmission service for both affiliates and non-affiliates. Thus, the Commission is better able to guard against, and monitor for, abuses related to a Transmission Owner's priority to use internal system capacity for native load to make off-system sales.

Fourth, the Commission examined the issue of strategic curtailments. The Commission found that TVA, not Applicants, curtails generation through TLRs.⁶⁴ TVA will continue in this role under Applicants' proposal.

Fifth, the Commission looked at the issue of gaming of OASIS. The Commission required that SPP would be responsible for the ATC calculation and posting of ATC, and would have no incentive to game the system.⁶⁵ Applicants will gain these functions under the current proposal subject to the enhanced transparency requirements implemented in Order No.890, as discussed above. Also, TVA would continue to determine AFC. Thus, gaming of OASIS should no longer be a concern.

d. Applicants' Replacement for the ITO Will Not Adversely Affect Rates.

As noted above, Applicants' filing will not adversely affect rates. There will be no adverse change in transmission rates charged to Applicants' customers due to the termination of the ITO Agreement. Applicants will continue to offer the current hold harmless commitments to Existing Customers and to maintain the Midwest ISO settlement with KU requirements

⁶² *Id.* at PP 88-89.

⁶³ *Id.* at PP 90-91.

⁶⁴ *Id.* at P 92.

⁶⁵ *Id.* at PP 93-94.

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customers, and will continue to charge Attachment O transmission rates and their existing ancillary service rates.

e. Applicants' Replacement for the ITO Will Not Adversely Affect Regulation.

In the context of a merger application under FPA Section 203, Order No. 642 provided that the Commission would evaluate the effect of a merger on regulation both at a federal and state level. There are no such concerns presented by the present filing. Applicants' proposal will neither change the state/federal regulatory jurisdictional boundaries nor create a regulatory gap. Also, the Commission's concern that state regulators should not be divested of authority to act on mergers of traditional, vertically-integrated utilities with captive retail (as well as wholesale) customers is not applicable here.⁶⁶ Furthermore, upon Applicants' replacement of the performance of the ITO functions, they will continue to be subject to the KPSC's jurisdiction with respect to retail gas and electric rates, service, and operation. Accordingly, Applicants' proposal will have no adverse effect on state regulation.⁶⁷

D. EFFECT ON RELIABILITY

Applicants' proposal will not have any adverse effect on reliability. As explained above, TVA will continue to be the NERC-certified Reliability Coordinator for the Applicants' control area. TVA will continue to fulfill its Reliability Coordinator duties in a manner consistent with NERC Standards, industry practices and business processes.

V. INFORMATION REQUIRED UNDER 18 C.F.R. PART 35

A. ACTION DATE AND PROPOSED EFFECTIVE DATE

As discussed in Applicants' request for expedited action set forth above, Applicants request Commission action on this filing by no later than the July 2010 Commission Meeting. Applicants also request a preliminary approval of the proposed ITO replacement within 120 days of this filing to allow sufficient time for the operational cutover. These expedited actions by the Commission are necessary to ensure that Applicants and the SPP may effectively coordinate the transition of ITO functions currently performed by SPP, prior to the August 31, 2010 expiration of the ITO Agreement.

⁶⁶ See Order No. 642, FERC Stats. & Regs. at 31,914-15.

⁶⁷ See *Madison Gas and Elec. Co.*, 106 FERC ¶ 61,098, P 20 (2004); *Texas-New Mexico Power Co., Southern New Mexico Elec. Co.*, 105 FERC ¶ 61,028, P 22 (2003); *Ameren Energy Generating Co., Union Elec. Co., d/b/a AmerenUE*, 103 FERC ¶ 61,128, P 60 (2003).

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Applicants seek an effective date for the rates proposed herein as of the date the Commission accepts this submittal for filing. Applicants request waiver, to the extent necessary, of the Commission's 60-day or 120-day notice requirements (as may be applicable) in order to permit the rates to take effect upon the Commission's acceptance of this submittal for filing.⁶⁸

B. SERVICE

A copy of this transmittal letter and all exhibits has been served on the Kentucky Public Service Commission, as well all entities listed on the Commission's Official Service List. A list of all those to whom this transmittal letter and exhibits has been sent is attached hereto as Exhibit 3. To avoid submitting large volume of paper copies of this filing, Applicants are submitting such copies on a diskette (in PDF format) to those listed on the service list.

C. COMMUNICATIONS

Applicants request that all notices and correspondence related to this filing be sent to the following individuals, and that the Secretary include these individuals on the official service list for these proceedings.

Jennifer Keisling
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and Kentucky Utilities Company
220 West Main Street
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(502) 627-2557
(502) 627-3367 (fax)

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(202) 274-2950
(202) 654-5659 (fax)

D. ADDITIONAL MATTERS AND GENERAL WAIVERS

Per 18 C.F.R. § 35.13(b)(7), Applicants state that no expenses or costs associated with their proposal have been alleged or judged in any administrative or judicial proceedings to be illegal, duplicative, or unnecessary costs that are demonstrably the product of discriminatory employment practices.

Applicants respectfully request a waiver of any requirements of 18 C.F.R. § 35.13 that have not been fulfilled by this filing. The tariff sheets filed herein do not contemplate a change

⁶⁸ See 18 C.F.R. § 35.3.

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in rates other than what is necessary to effectuate Applicants' replacement of the ITO. Furthermore, as noted throughout this filing, the proposed rates have been approved by the Commission as *pro forma* rates, or reflect rate and tariff terms accepted by the Commission in other proceedings.

VI. CONCLUSION

WHEREAS, as set forth above, and:

With regard to FPA Section 203 specifically, Applicants request that the Commission make the following findings:

1. That Applicants' proposal satisfies the Merger Conditions and the Midwest ISO Exit Order regarding vertical market power issues and independence; and
2. That Applicants' commitment to the KU requirements customers not to re-pancake transmission rates as set forth in the Midwest ISO Exit Settlement, after the termination of the ITO Agreement: (i) continues to satisfy the Merger Conditions; and (ii) mitigates any concerns regarding horizontal market power in the KU destination market that may have resulted from the company's prior mergers.

With regard to FPA Section 205, specifically, Applicants request that the Commission:

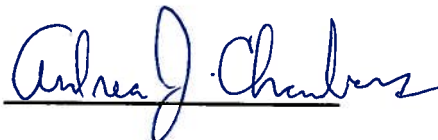
1. Accept for filing a revised OATT (which has been modified to delete the ITO Agreement and Attachment P, and to reassign ITO functions to Applicants); and
2. Approve Applicants' proposed replacement for the ITO arrangement with SPP as just and reasonable.

In addition, Applicants request that the Commission review this filing on an expedited basis, and issue a conditional approval of the proposed ITO replacement within 120 days of this filing. This conditional approval is necessary to provide LG&E/KU with sufficient time to hire staff, conduct training, and implement software changes. LG&E/KU must start this process by February 2010 to allow sufficient time to safely and reliably cut over to the new system by September 1, 2010. Finally, Applicants request that the Commission issue a final decision on the merits of this case by no later than the July 2010 Commission Meeting.

**TROUTMAN
SANDERS**

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Respectfully submitted,



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Electric Company and Kentucky Utilities Company*

Date: October 30, 2009
Washington, D.C.

CERTIFICATE OF SERVICE

I hereby certify that on this 30th day of October, 2009, I have served a copy of the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.



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