BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

February 13, 2007

IN RE:	)	
	)	
PETITION OF KENTUCKY UTILITIES COMPANY FOR AN ORDER AUTHORIZING THE ISSUANCE OF SECURITIES AND THE ASSUMPTION OF OBLIGATIONS	)))	**DOCKET NO. 06-00235**

ORDER APPROVING FINANCING TRANSACTION

This matter came before Director Eddie Roberson, Director Pat Miller and Director Ron Jones of the Tennessee Regulatory Authority (the "Authority" or "TRA"), the voting panel assigned to this docket, at a regularly scheduled Authority Conference held on November 6, 2006 for consideration of the *Petition* of Kentucky Utilities Company ("KUC" or the "Company") for an Order authorizing the issuance of securities and the assumption of obligations, pursuant to Tenn. Code Ann. § 65-4-109 (2004). On January 12, 2007 KUC filed an *Amendment to Petition* ("*Amendment*") and this matter was again placed before the panel at a regularly scheduled Authority Conference held on January 23, 2007.

The *Petition*

KUC is an electric utility serving customers in Kentucky and Virginia primarily, with five customers in the State of Tennessee. On September 14, 2006, KUC filed a *Petition* with the Authority requesting approval to (1) obtain long-term unsecured debt[1] from an affiliate within the E.ON AG

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[1] The Authority has previously authorized KUC's entry into debt obligations in Docket No. 06-00140. *See In re: Petition of Kentucky Utilities Company for an Order Authorizing the Issuance of Securities and the Assumption of Obligations,* Docket No. 06-00140, *Order Approving Financing Transaction* (June 26, 2006). KUC subsequently issued that tax-exempt financing. Two similar allocations for $13,266,950 each were made to KUC in 2005, and approved by the Authority in Docket No. 05-00144 and Docket No. 05-00249. *See In re: Petition of Kentucky Utilities Company for an Order Authorizing the Issuance of Securities and the Assumption of Obligations*, Docket No. 05-00144, *Order Approving Financing Transactions* (June 20, 2005) and *In re: Petition of Kentucky Utilities Company for an Order Authorizing the Issuance of Securities and the Assumption of Obligations*, Docket No. 05-00249 (October 19, 2005). Those tax-exempt financing were issued as well. The Authority also approved KUC's petition in Docket No. 06-00248. *See In re: Petition of Kentucky Utilities Company for an Order Authorizing the Issuance of Securities and the Assumption of Obligations*, Docket No. 06-00248 (October 30, 2006).

("E.ON") holding company system in order to defease and discharge its one remaining series of outstanding external taxable debt, and (2) issue new, unsecured tax-exempt pollution control debt in order to refund one series of secured, tax-exempt pollution control debt.

According to the *Petition*, E.ON U.S. LLC ("E.ON US") and E.ON US Holding GmbH are indirect subsidiaries of E.ON. KUC is a wholly-owned subsidiary of E.ON US. Fidelia Corporation ("Fidelia"), a finance subsidiary of E.ON U.S. Holding GmbH, lends money to companies in the E.ON holding company system, including KUC.

As set out in the *Petition,* KUC will borrow money from Fidelia in an amount not to exceed $53,000,000 for the purpose of defeasing the outstanding 7.92% First Mortgage Bonds, Series P, due May 15, 2007. Pursuant to the terms of the initial financing documents, the Series P First Mortgage Bonds are not redeemable and can only be defeased until their discharge at maturity. The defeasance requires KUC to deposit with the bond trustee an amount of cash or U.S. Treasury securities which, upon maturity of the bonds, will be sufficient to cover both principal and accrued interest.

To facilitate the transaction, KUC will issue unsecured notes to Fidelia with a final maturity not to exceed 30 years. A note will be executed by KUC each time a loan is made by Fidelia to the Company stating the interest rate, maturity date and payment terms. Issuance expenses for the loans will not exceed, in total, the sum of $50,000. The interest rate on the Fidelia loan will be set at the time the note is issued and will depend on the maturity date affixed. KUC states that borrowing will only ensue if the interest rate on the loan will result in an equal or lower cost of borrowing than KUC could otherwise obtain in the capital markets; thus, ensuring that it will not pay more for a loan from an affiliate than it would pay for a similar loan in the capital markets.

The *Petition* states that the interest rate on the note would be the lower of: (a) the average of three quotes obtained by the affiliate company from international investment banks for an unsecured bond issued by E.ON for the applicable term of the loan, and (b) the lowest of three quotes obtained by

KUC from international investment banks for an unsecured bond issued by KUC with the applicable term of the loan. In connection with the issuance of the debt, KUC may enter into one or more interest rate hedging agreements (T-bill lock, swap or similar agreement, collectively the "Hedging Facility" or "Hedging Facilities") either with an E.ON affiliate or with a bank or financial institution.

Additionally in the *Petition,* KUC describes a series of transactions through which it will finance a portion of its pollution control project on a tax-exempt basis. KUC will redeem the $54,000,000 principal amount of County of Carroll, Kentucky Solid Waste Disposal Facilities Revenue Bonds (Kentucky Utilities Company Project) 1994 Series A, due November 1, 2024 ("Carroll County 1994 Series A Bonds" or the "Existing Bonds"), secured by KUC's First Mortgage Bonds, Series 10. Specifically, KUC will assume certain obligations under various agreements in connection with the issuance of one or more series of new County of Carroll, Kentucky Environmental Facilities Revenue Bonds (the "Refunding Bonds"). As to refinancing of the Existing Bonds, KUC will assume certain obligations under one or more Loan Agreements with Carroll County, and may enter into Guarantee Agreements undertaking payment of all or any part of the obligations under the Refunding Bonds for the benefit of the holders of such Bonds. The proceeds from the sale of the loan will be used to provide financing for a portion of the Refunding Bonds.

The payments made by KUC under the Loan Agreements for one or more series of Refunding Bonds, together with other available funds, will be sufficient to pay the principal and interest on such Refunding Bonds. KUC will enter into one or more interest rate Hedging Facilities with a bank or financial institution (the "Counterparty"). The Hedging Facility will be an interest rate agreement designed to allow KUC to actively manage and limit its exposure to variable interest rates or to lower its overall borrowing costs on any fixed rate Refunding Bond. The Hedging Facility will set forth the specific terms by which KUC will pay the Counterparty's payments and/or fees for limiting its interest rate exposure or lowering fixed rate borrowing costs, and any other terms and conditions of any rights or obligations in accordance therewith.

The terms of each financing instrument will be negotiated by KUC with the respective Bank, Facility Provider or Counterparty, and will be arranged at the most favorable terms that are able to be secured by KUC. The aggregate outstanding principal amount of the obligations of KUC, at any time under all of the financing instruments, will not exceed the original aggregate principal amount of the Refunding Bonds ($54,000,000), plus accrued but unpaid interest and premium, if any, on such bonds.

The November 6, 2006 Authority Conference

Tenn. Code Ann. § 65-4-109 (2004) states:

> No public utility shall issue any stocks, stock certificates, bonds, debentures, or other evidences of indebtedness payable in more than one (1) year from the date thereof, until it shall have first obtained authority from the authority for such proposed issue. It shall be the duty of the authority after hearing to approve any such proposed issue maturing more than one (1) year from the date thereof upon being satisfied that the proposed issue, sale and delivery is to be made in accordance with law and the purpose of such be approved by the authority.

At a regularly scheduled Authority Conference held on November 6, 2006, the voting Panel assigned to this docket voted unanimously to approve the *Petition* contingent upon its approval by the Kentucky Public Service Commission and the State Corporation Commission of Virginia, and subject further to the filing requirements approved by those Commissions, after making the following findings:

1. The financing transaction proposed by the parties is subject to Authority approval pursuant to Tenn. Code Ann. § 65-4-109 (2004) and is being made in accordance with the laws enforceable by the Authority;

2. That the purposes of the above-described transaction are in the public interest such that, but not limited to, the fact that the reduction in administrative costs for KUC will allow the utility to control and minimize costs to its consumers; and

3. The Panel also noted that its decision is not intended to create any liability on the part of the TRA, the State of Tennessee, or any public subdivision thereof.

The *Amendment to Petition*

The *Amendment* filed on January 12, 2007, reflects a change in the formula for the Best Rate Methodology used in KU's internal financings related to proposed and future loans with Fidelia Corporation, as requested by the Kentucky Public Service Commission ("KPSC"). The Best Rate Method is applied to prevent KU from paying more for a loan from Fidelia, an affiliate of KU, than it would pay in the capital markets for a similar loan. The *Amendment* changes one word in paragraph 7, page 6, of the *Petition* that was filed on September 14, 2006 in this docket. In clause (b) of paragraph 7, the word "unsecured" is changed to "secured." The effect of this change, if any, will be neutral or result in lower costs for the benefit of rate payers.

The January 23, 2007 Authority Conference

At a regularly scheduled Authority Conference held on January 23, 2007, the voting Panel assigned to this docket voted unanimously to reconsider its action of November 6, 2006, and adopt the findings made at that conference and approve the *Petition*, as amended, contingent upon approval by the Virginia State Corporation Commission.[2]

IT IS THEREFORE ORDERED THAT:

1. The *Petition* of Kentucky Utilities Company for an Order authorizing the issuance of securities and the assumption of obligations, and subsequent amendment thereto, is approved contingent on its approval by the State Corporation Commission of Virginia and subject to the filing requirements approved by the Kentucky Public Service Commissions and the State Corporation Commission of Virginia.

2. Kentucky Utilities Company is authorized to issue and deliver its unsecured notes to Fidelia Corporation in an aggregate principal amount not to exceed $53,000,000 as set forth in its *Petition* and discussed herein.

[2] The Kentucky Public Service Commission has approved the application as amended. *See In the Matter of: The Application of Kentucky Utilities Company for an Order Authorizing the issuance of Securities and the Assumption of Obligations*, Case No. 2006-00390, *Order* (January 22, 2007).

3. Kentucky Utilities Company is authorized to execute, deliver and perform the obligations of Kentucky Utilities Company under, *inter alia*, the Loan Agreements with the Fidelia Corporation, the Notes and such other agreements and documents as set forth in the *Petition* and discussed herein, and to perform the transactions contemplated by such agreements.

4. Kentucky Utilities Company is authorized, with regard to the Refunding Bonds, to execute, deliver and perform the obligations of Kentucky Utilities Company under, *inter alia*, the Loan Agreements with Carroll County, Kentucky and under any Guarantees, remarketing agreements, hedging agreements, auction agreements, bond issuance agreements, Credit Agreements, Facilities and such other agreements and documents as set forth in the *Petition* and discussed herein, and to perform the transactions contemplated by such agreements.

5. Subsequent to the issuance of the securities, Kentucky Utilities Company shall file with the Tennessee Regulatory Authority any additional information regarding the issuance of the securities that is required by Kentucky Public Service Commission and the State Corporation Commission of Virginia.

6. The authorization given hereby shall not be used by any party, including but not limited to, any lending party, for the purpose of inferring an analysis or assessment of the risks involved. Nothing herein creates or is intended to create any liability on the part of the Tennessee Regulatory Authority, the State of Tennessee, or any political subdivision thereof.

Eddie Roberson, Director

Pat Miller, Director

Ron Jones, Director