UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Nora Mead Brownell, and Suedeen G. Kelly.

Cincinnati Gas and Electric Company, d/b/a Duke Energy Ohio — Docket No. EL06-66-000

Union Light, Heat and Power Company, d/b/a Duke Energy Kentucky

ORDER GRANTING PETITION FOR DECLARATORY ORDER, AS CONDITIONED

(Issued May 26, 2006)

1. On April 18, 2006, Cincinnati Gas and Electric Company d/b/a Duke Energy Ohio (Duke Energy Ohio) and Union Light, Heat and Power Company d/b/a Duke Energy Kentucky (Duke Energy Kentucky) (collectively, Applicants) filed a petition for declaratory order requesting the Commission find that the payment of dividends from capital accounts will not violate section 305(a) of the Federal Power Act (FPA).[1] For the reasons stated below, we will grant, as conditioned below, Applicants' petition for declaratory order.

Background

2. On July 12, 2005, Duke Energy Corporation and Cinergy Corporation (Cinergy) filed an application pursuant to section 203 of the FPA requesting Commission approval of their proposed merger which resulted in Cinergy becoming a wholly-owned subsidiary of Duke Energy Corporation. Applicants state that Duke Energy Ohio continues to be wholly-owned by Cinergy, and Duke Energy Kentucky continues to be wholly-owned by Duke Energy Ohio.

3. Applicants state that under generally accepted accounting principles, mergers resulting in a change of control must be accounted for by using purchase accounting. Under purchase accounting, if the acquiring company's purchase price exceeds the fair

[1] 16 U.S.C. § 825d(a) (2000).

market value of the acquired company's net assets, this excess is recorded as goodwill on the acquiring company's balance sheet. Applicants state that the goodwill, and any other adjustments to the values of assets or liabilities of the acquired entity on the acquiring company's balance sheet, must be reviewed to determine whether it must then be assigned or "pushed-down" to the balance sheet of any acquired subsidiaries to the extent those subsidiaries file periodic reports with the Securities and Exchange Commission.

4. Applicants state that Duke Energy Ohio has determined that it must apply push-down accounting based on discussions with its independent auditor, Deloitte & Touche, LLP. Applicants note that a determination as to the applicability of push-down accounting to Duke Energy Kentucky has not been concluded, but push-down accounting potentially could be applied to Duke Energy Kentucky as well. Therefore, Applicants request a Commission ruling with respect to both companies, with the understanding that the ruling will apply to Duke Energy Kentucky only if push-down accounting is applied and its retained earnings account is reduced to zero as of the date of the closing of the merger.

5. Applicants maintain that push-down accounting will result in one-time adjustments to certain of Applicants' assets and liabilities as of the merger closing. They state that prior to the closing of the merger, Duke Energy Ohio's retained earnings account was approximately $671 million and Duke Energy Kentucky's retained earnings account was approximately $176 million. Although the amount of dividends declared is expected to be well below the amounts that were in Applicants' retained earnings accounts immediately prior to the merger, it is expected that Applicants may be unable to pay dividends from their retained earnings after the balance in such accounts is eliminated due to purchase accounting.[2]

6. Applicants argue that the payment of dividends from capital accounts, subject to the conditions set forth in the petition, detailed below, is consistent with prior Commission precedent and permissible under section 305(a) of the FPA. Applicants state that this would include the payment of dividends on June 15, 2006, as well as the subsequent payment of dividends, provided that the total amount of dividends made from capital accounts does not exceed the amounts that were in Applicants' retained earnings accounts immediately prior to the closing of the merger.

7. First, Applicants state that the source of the dividends will be clearly identified. They contend that the dividends will be paid from capital accounts and will not exceed

[2] Duke Energy Ohio has had a consistent history of making quarterly dividend payments to Cinergy. Duke Energy Kentucky also routinely makes dividend payments to Duke Energy Ohio. These payments historically have been made annually or semi-annually.

the amounts in their retained earnings accounts immediately prior to the closing of the merger.

8. Second, Applicants assert that the dividends that will be paid from the capital accounts will not be excessive and will not impair their ability to conduct utility operations. Applicants state that they will not be paying more dividends than they would have been able to pay prior to the time of the merger when their retained earnings accounts were adjusted down to zero. Thus, Applicants contend that the actual funds that will be used to pay the dividends are no different after the closing of the merger than before. The only difference is the account from which the dividends will be made.

9. Third, Applicants maintain that shareholders will not be harmed by the proposed issuance of dividends from capital accounts because they will have the same shareholders both before and after the dividends are issued. Applicants state that dividends will be made consistent with their capital structure targets, which are designed to maintain credit metrics to support investment grade ratings.

Notice of Filing

10. Notice of Applicants April 18, 2006, filing was published in the *Federal Register*, 71 Fed. Reg. 27,479 (2006), with interventions or protests due on or before May 11, 2006. None was filed.

Discussion

11. We will grant, as conditioned below, Applicants' petition.

Section 305(a) provides that:

> It shall be unlawful for any officer or director of any public utility to receive for his own benefit, directly or indirectly, any money or thing of value in respect of the negotiation, hypothecation, or sale by such public utility of any security issued or to be issued by such public utility, or to share in any of the proceeds thereof, or to participate in the making or paying of any dividends of such public utility from any funds properly included in capital accounts.[3]

12. The concerns underlying the enactment of section 305(a) included "that sources from which cash dividends were paid were not clearly identified and that holding companies had been paying out excessive dividends on the securities of their operating

[3] 16 U.S.C. § 825d(a) (2000).

companies. A key concern, thus, was corporate officials raiding corporate coffers for their personal financial benefit."[4]

13. Applicants are proposing to realign their capital structure through issuance of dividends from certain capital accounts. Applicants have clearly identified the source from which payment will be made. The dividends will be paid from capital accounts and will not exceed in aggregate the amount in the Applicants' retained earnings account immediately prior to the closing of the merger. Applicants will not be paying more dividends than they would have been able to pay prior to the time of the merger when their retained earnings accounts were adjusted down to zero. The only difference is the account from which the dividends will be made. In addition, we will require Applicants to maintain a minimum equity balance equal to 30 percent of total capital.[5] On this basis, any dividends paid will not be excessive.

14. Finally, the issuance of dividends from capital accounts will not harm shareholders. Applicants will have the same shareholders both before and after the dividends are issued. The dividends will be made consistent with Applicants' capital structure targets, which are designed to maintain credit metrics to support investment grade ratings.

15. For these reasons, and under the circumstances of this case, we will grant the petition, as conditioned above, and accordingly find that section 305(a) of the FPA is not a bar to the payment of dividends from certain capital accounts described above.

The Commission orders:

(A) Applicants' petition for declaratory order, as conditioned, is hereby granted, as discussed in the body of this order.

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[4] *Entergy Louisiana Inc.*, 114 FERC ¶ 61,060 at P 12 (2006); *Exelon Corporation*, 109 FERC ¶ 61,172 at P 8 (2004); *ALLETE, INC.*, 107 FERC ¶ 61,041 at P 10 (2004).

[5] *See, e.g.*, *Niagara Mohawk Holdings, Inc.*, 95 FERC ¶ 61,381 at 62,416 (2001).

(B) Applicants must inform the Commission of any change in circumstances that would reflect a departure from the facts the Commission relied upon in granting the petition.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.