

CINERGY CORP.

2009 Second Quarter Financial Report

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CINERGY CORP.

JUNE 30, 2009

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CINERGY CORP.
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In millions)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Operating Revenues				
Regulated electric	\$ 1,100	\$ 801	\$ 2,304	\$ 1,657
Non-regulated electric and other	139	491	325	930
Regulated natural gas	94	113	394	470
Total operating revenue	1,333	1,405	3,023	3,057
Operating Expenses				
Fuel used in electric generation and purchased power - regulated	408	255	853	534
Fuel used in electric generation and purchased power - non-regulated	70	155	155	322
Cost of natural gas and coal sold	42	60	249	322
Operation, maintenance and other	358	351	740	677
Depreciation and amortization	198	195	397	389
Property and other taxes	81	79	183	172
Total operating expenses	1,157	1,095	2,577	2,416
Gains on Sales of Other Assets and Other, net	1	33	5	49
Operating Income	177	343	451	690
Other Income and Expenses				
Equity in (loss) earnings of unconsolidated affiliates	(5)	6	(6)	14
Other income and expenses, net	29	36	48	68
Total other income and expenses	24	42	42	82
Interest Expense	68	64	144	129
Income From Continuing Operations Before Income Taxes	133	321	349	643
Income Tax Expense from Continuing Operations	48	110	124	225
Income From Continuing Operations	85	211	225	418
Income From Discontinued Operations, net of tax	-	16	-	24
Net Income	85	227	225	442
Less: Net Income Attributable to Noncontrolling Interests	-	-	-	-
Net Income Attributable to Cinergy Corp.	\$ 85	\$ 227	\$ 225	\$ 442

See Notes to Unaudited Consolidated Financial Statements

CINERGY CORP.
CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In millions)

	June 30, 2009	December 31, 2008
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 66	\$ 208
Receivables (net of allowance for doubtful accounts of \$18 at June 30, 2009 and \$20 at December 31, 2008)	980	916
Inventory	478	405
Other	714	584
Total current assets	2,238	2,113
Investments and Other Assets		
Restricted funds held in trust	24	25
Investments in equity method unconsolidated affiliates	365	383
Goodwill	4,459	4,460
Intangibles, net	579	639
Notes receivable	93	93
Other	554	489
Total investments and other assets	6,074	6,089
Property, Plant and Equipment		
Cost	20,333	19,574
Less accumulated depreciation and amortization	5,424	5,192
Net property, plant and equipment	14,909	14,382
Regulatory Assets and Deferred Debits		
Deferred debt expense	72	68
Regulatory assets related to income taxes	181	169
Other	1,050	1,062
Total regulatory assets and deferred debits	1,303	1,299
Total Assets	\$ 24,524	\$ 23,883

See Notes to Unaudited Consolidated Financial Statements

CINERGY CORP.
CONSOLIDATED BALANCE SHEETS - (Continued)
(Unaudited)
(In millions, except share and per-share amounts)

	June 30, 2009	December 31, 2008
LIABILITIES AND EQUITY		
Current Liabilities		
Accounts payable	\$ 573	\$ 651
Notes payable	972	1,193
Taxes accrued	179	211
Interest accrued	81	69
Current maturities of long-term debt	263	313
Other	264	308
Total current liabilities	2,332	2,745
Long-term Debt	5,658	4,772
Deferred Credits and Other Liabilities		
Deferred income taxes	2,607	2,380
Investment tax credits	27	29
Accrued pension and other post-retirement benefit costs	980	1,283
Asset retirement obligations	62	58
Other	1,026	1,029
Total deferred credits and other liabilities	4,702	4,779
Commitments and Contingencies		
Equity		
Common Stock, \$0.01 par value; 1,000 shares authorized, 100 shares issued and outstanding at June 30, 2009 and December 31, 2008	-	-
Additional paid-in capital	10,978	10,977
Retained earnings	1,036	811
Accumulated other comprehensive loss	(197)	(217)
Total Cinergy Corp. shareholders' equity	11,817	11,571
Noncontrolling Interests	15	16
Total equity	11,832	11,587
Total Liabilities and Equity	\$ 24,524	\$ 23,883

See Notes to Unaudited Consolidated Financial Statements

CINERGY CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In millions)

	Six Months Ended	
	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 225	\$ 442
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	400	392
Gains on sales of other assets	(6)	(72)
Impairment charges	6	-
Deferred income taxes	195	62
Equity in loss (earnings) of unconsolidated affiliates	6	(14)
Contributions to qualified pension plans	(394)	-
Accrued pension and other post-retirement benefit costs	27	47
(Increase) decrease in		
Net realized and unrealized mark-to-market and hedging transactions	(2)	(182)
Receivables	245	118
Inventory	(73)	(12)
Other current assets	(119)	(23)
Increase (decrease) in		
Accounts payable	(42)	59
Taxes accrued	58	144
Other current liabilities	1	14
Regulatory asset/liability deferrals	(11)	(17)
Other assets	39	15
Other liabilities	(9)	(81)
Net cash provided by operating activities	<u>546</u>	<u>892</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(758)	(822)
Investment expenditures	(67)	(1)
Acquisitions, net of cash acquired	(114)	-
Purchases of available-for-sale securities	(15)	(9)
Proceeds from sales and maturities of available-for-sale securities	15	8
Net proceeds from the sales of other assets and sales of and collections on notes receivable	43	76
Purchases of emission allowances	(38)	(24)
Sales of emission allowances	15	79
Notes due from affiliate, net	(320)	-
Change in restricted cash	(48)	34
Other	(6)	9
Net cash used in investing activities	<u>(1,293)</u>	<u>(650)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of long-term debt	1,240	-
Redemption of long-term debt	(412)	(145)
Notes payable and commercial paper	-	(119)
Notes payable to affiliate, net	(215)	-
Other	(8)	(1)
Net cash provided by (used in) financing activities	<u>605</u>	<u>(265)</u>
Net decrease in cash and cash equivalents	(142)	(23)
Cash and cash equivalents at beginning of period	<u>208</u>	<u>109</u>
Cash and cash equivalents at end of period	<u>\$ 66</u>	<u>\$ 86</u>
Supplemental Disclosures		
Significant non-cash transactions:		
Accrued capital expenditures	\$ 114	\$ 58
Reclassification of money pool borrowings to long-term debt	\$ -	\$ 150

See Notes to Unaudited Consolidated Financial Statements

CINERGY CORP.
CONSOLIDATED STATEMENTS OF EQUITY AND COMPREHENSIVE INCOME
(Unaudited)
(In millions)

	Accumulated Other Comprehensive Income (Loss)									
	Common Stock	Additional Paid-in Capital	Retained Earnings	Foreign Currency Adjustments	Net Gains (Losses) on Cash Flow Hedges	Other	Pension and OPEB-related Adjustments to AOCI	Common Stockholders' Equity	Noncontrolling Interests	Total Equity
Balance December 31, 2007	\$ -	\$ 10,786	\$ 421	\$ 1	\$ (33)	\$ 1	\$ (21)	\$ 11,155	\$ 18	\$ 11,173
Net income	-	-	442	-	-	-	-	442	-	442
Other Comprehensive Income										
Foreign currency translation adjustment (c)	-	-	-	(2)	-	-	-	(2)	-	(2)
Unrealized losses on available-for-sale securities (d)	-	-	-	-	-	(4)	-	(4)	-	(4)
Cash flow hedges (a)	-	-	-	-	(1)	-	-	(1)	-	(1)
SFAS No. 158 amortization (b)	-	-	-	-	-	-	1	1	-	1
Total comprehensive income								436	-	436
Other	-	2	-	-	-	-	-	2	1	3
Balance June 30, 2008	\$ -	\$ 10,788	\$ 863	\$ (1)	\$ (34)	\$ (3)	\$ (20)	\$ 11,593	\$ 19	\$ 11,612
Balance December 31, 2008	\$ -	\$ 10,977	\$ 811	\$ (1)	\$ (14)	\$ -	\$ (202)	\$ 11,571	\$ 16	\$ 11,587
Net income	-	-	225	-	-	-	-	225	-	225
Other Comprehensive Income										
Foreign currency translation adjustment	-	-	-	(8)	-	-	-	(8)	-	(8)
Cash flow hedges (a)	-	-	-	-	12	-	-	12	-	12
Pension and OPEB-related Adjustments to AOCI (b)	-	-	-	-	-	-	16	16	-	16
Total comprehensive income								245	-	245
Other	-	1	-	-	-	-	-	1	(1)	-
Balance June 30, 2009	\$ -	\$ 10,978	\$ 1,036	\$ (9)	\$ (2)	\$ -	\$ (186)	\$ 11,817	\$ 15	\$ 11,832

- (a) Net of \$6 tax expense in 2009 and \$1 tax benefit in 2008.
(b) Net of \$7 tax expense in 2009 and \$2 tax expense in 2008.
(c) Net of \$2 tax benefit in 2008.
(d) Net of \$4 tax benefit in 2008.

See Notes to Unaudited Consolidated Financial Statements

Notes to Unaudited Consolidated Financial Statements

1. Basis of Presentation

Nature of Operations and Basis of Consolidation. Cinergy Corp. (collectively with its subsidiaries, Cinergy), a wholly-owned subsidiary of Duke Energy Corporation (Duke Energy), is an energy company primarily located in Ohio, Indiana, Kentucky and Texas. Cinergy directly or indirectly owns all outstanding common stock of its regulated public utility subsidiaries, Duke Energy Ohio, Inc. (Duke Energy Ohio), which includes Duke Energy Ohio's wholly-owned public utility subsidiary, Duke Energy Kentucky, Inc. (Duke Energy Kentucky), and Duke Energy Indiana, Inc. (Duke Energy Indiana). Additionally, Cinergy owns Cinergy Investments, Inc. (Investments), a non-regulated investment holding company involved in cogeneration and energy efficiency investments, renewable energy and energy marketing. Prior to July 1, 2008, Cinergy owned Duke Energy Shared Services, which provided administrative, management and support services to Cinergy's subsidiaries.

These Unaudited Consolidated Financial Statements include, after eliminating intercompany transactions and balances, the accounts of Cinergy and all majority-owned subsidiaries where Cinergy has control and those variable interest entities where Cinergy is the primary beneficiary. These Unaudited Consolidated Financial Statements also reflect Cinergy's proportionate share of certain generation and transmission facilities in Ohio, Indiana and Kentucky.

These Unaudited Consolidated Financial Statements have been prepared in accordance with generally accepted accounting principles (GAAP) in the United States of America (U.S.) for interim financial information. Accordingly, these Unaudited Consolidated Financial Statements do not include all of the information and notes required by GAAP in the U.S. for annual financial statements. Because the interim Unaudited Consolidated Financial Statements and Notes do not include all of the information and notes required by GAAP in the U.S. for annual financial statements, the Unaudited Consolidated Financial Statements and other information included in this quarterly report should be read in conjunction with the Consolidated Financial Statements and Notes in Cinergy's Year-End Financial Report for the year ended December 31, 2008.

These Unaudited Consolidated Financial Statements reflect all normal recurring adjustments that are, in the opinion of management, necessary to fairly present Cinergy's financial position and results of operations. Amounts reported in the interim Unaudited Consolidated Statements of Operations are not necessarily indicative of amounts expected for the respective annual periods due to the effects of seasonal temperature variations on energy consumption, regulatory rulings, the timing of maintenance on electric generating units, changes in market valuations, changing commodity prices and other factors.

Use of Estimates. To conform to GAAP in the U.S., management makes estimates and assumptions that affect the amounts reported in the Unaudited Consolidated Financial Statements and Notes. Although these estimates are based on management's best available information at the time, actual results could differ.

Reclassifications. Certain prior period amounts on the Unaudited Consolidated Financial Statements have been reclassified in connection with the adoption of Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 160, "Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51," (SFAS No. 160) on January 1, 2009, as discussed in Note 15, the effects of which require retrospective application to the Unaudited Consolidated Financial Statements.

Unbilled Revenue. Revenues on sales of electricity and gas are recognized when either the service is provided or the product is delivered. Unbilled retail revenues are estimated by applying an average revenue per kilowatt-hour or per thousand cubic feet (Mcf) for all customer classes to the number of estimated kilowatt-hours or Mcf's delivered but not billed. Unbilled wholesale energy revenues are calculated by applying the contractual rate per megawatt-hour (MWh) to the number of estimated MWh delivered but not yet billed. Unbilled wholesale demand revenues are calculated by applying the contractual rate per megawatt (MW) to the MW volume delivered but not yet billed. The amount of unbilled revenues can vary significantly from period to period as a result of numerous factors, including seasonality, weather, customer usage patterns and customer mix. Unbilled revenues, which are primarily recorded as Receivables on the Consolidated Balance Sheets, primarily relate to wholesale sales within Cinergy's non-regulated businesses and were approximately \$63 million and \$57 million at June 30, 2009 and December 31, 2008, respectively. Additionally, Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky sell, on a revolving basis, nearly all of their retail and wholesale accounts receivable and related collections to Cinergy Receivables Company, LLC (Cinergy Receivables), a bankruptcy remote, special purpose entity that is a wholly-owned limited liability company of Cinergy. The securitization transaction was structured to meet the criteria for sale treatment under SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities—a replacement of FASB Statement No. 125" (SFAS No. 140), and, accordingly, Cinergy does not consolidate Cinergy Receivables and the transfers of receivables are accounted for as sales. Receivables for unbilled revenues of approximately \$192 million and \$266 million at June 30, 2009 and December 31, 2008, respectively, related to retail and wholesale accounts receivable at Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky were included in the sales of accounts receivable to Cinergy Receivables. See Note 17 for additional information regarding Cinergy Receivables.

Other Regulatory Assets and Deferred Debits. The state of Ohio passed comprehensive electric deregulation legislation in 1999, and in 2000, the Public Utilities Commission of Ohio (PUCO) approved a stipulation agreement relating to Duke Energy Ohio's transition plan creating a Regulatory Transition Charge (RTC) designed to recover Duke Energy Ohio's generation-related regulatory assets and transition costs over a ten-year period beginning January 1, 2001 and ending December 2010. Accordingly, application of SFAS No. 71, "Accounting for Certain Types of Regulation" (SFAS No. 71), was discontinued for the generation portion of Duke Energy Ohio's business at that time (see below for subsequent reapplication of SFAS No. 71 to certain portions of Duke Energy Ohio's business). Duke Energy Ohio has a RTC related regulatory asset balance of approximately \$107 million and \$138 million as of June 30, 2009 and December 31, 2008, respectively, which is classified in Other within Regulatory Assets and Deferred Debits on the Consolidated Balance Sheets.

Reapplication of SFAS No. 71 to Portions of Generation in Ohio. Duke Energy Ohio's generation operations include generation assets located in Ohio that are dedicated to serve Ohio native load customers. These assets, as excess capacity allows, also generate revenues through sales outside the native load customer base, and such revenue is termed non-native.

Prior to December 17, 2008, certain portions of Duke Energy Ohio's business did not apply the provisions of SFAS No. 71 due to the comprehensive electric deregulation legislation passed by the state of Ohio in 1999. As described further below, effective December 17, 2008, the PUCO approved Duke Energy Ohio's Electric Security Plan (ESP), which resulted in the reapplication of SFAS No. 71 to certain portions of Duke Energy Ohio's operations as of that date.

From January 1, 2005 through December 31, 2008, Duke Energy Ohio had been operating under a Rate Stabilization Plan (RSP), which was a market-based standard service offer. Although the RSP contained certain trackers that enhanced the potential for cost recovery, there was no assurance of stranded cost recovery upon the expiration of the RSP on December 31, 2008 since it was initially anticipated that, upon the expiration of the RSP, there would be a move to full competitive markets. Accordingly, certain portions of Duke Energy Ohio's business did not apply the provisions of SFAS No. 71 to any of its generation operations prior to December 17, 2008. As discussed further in Note 10, in April 2008, new legislation (SB 221) was passed in Ohio and signed by the Governor of Ohio on May 1, 2008. The new law codified the PUCO's authority to approve an electric utility's standard service offer either through an ESP or a Market Rate Option (MRO).

Notes to Unaudited Consolidated Financial Statements

The MRO is a price determined through a competitive bidding process. On July 31, 2008, Duke Energy Ohio filed an ESP, and with certain amendments, the ESP was approved by the PUCO on December 17, 2008. The ESP became effective on January 1, 2009.

In connection with the approval of the ESP, Duke Energy Ohio reassessed the applicability of SFAS No. 71 to the portion of its generation operations that did not apply SFAS No. 71 as SB 221 substantially increased the PUCO's oversight authority over generation in the state of Ohio, including giving the PUCO complete approval of generation rates and the establishment of an earnings test to determine if a utility has earned significantly excessive earnings. Duke Energy Ohio determined that certain costs and related rates (riders) of Duke Energy Ohio's operations related to generation serving native load meet the criteria established by SFAS No. 71 for regulatory accounting treatment as SB 221 and Duke Energy Ohio's approved ESP enhanced the recovery mechanism for certain costs of its generation serving native load and increased the likelihood that these operations will remain under a cost recovery model for certain costs for the remainder of the ESP period.

Under the ESP, Duke Energy Ohio bills for its native load generation via numerous riders. SB 221 and the ESP resulted in the approval of an enhanced recovery mechanism for certain of these riders, which includes, but is not limited to, a price-to-compare fuel and purchased power rider and certain portions of a price-to-compare cost of environmental compliance rider. Accordingly, certain portions of Duke Energy Ohio's business began applying SFAS No. 71 to the corresponding RSP riders with a mechanism for enhanced recovery under the ESP on December 17, 2008. The remaining portions of Duke Energy Ohio's native load generation operations, revenues from which are reflected in rate riders for which the ESP does not specifically allow enhanced recovery, as well as all generation operations associated with non-native customers, including the Midwest gas-fired generation assets, continue to not apply regulatory accounting as those operations do not meet the criteria of SFAS No. 71. Moreover, generation remains a competitive market in Ohio and native load customers continue to have the ability to switch to alternative suppliers for their electric generation service. As customers switch, there is a risk that some or all of the regulatory assets will not be recovered through the established riders. Duke Energy Ohio will continue to monitor the amount of native load customers that have switched to alternative suppliers when assessing the probability of recovery of its regulatory assets established for its native load generation operations. See below for further discussion of customer switching.

Despite certain portions of the Ohio native load operations not being subject to the accounting provisions of SFAS No. 71, all of Duke Energy Ohio's native load operations' rates are subject to approval by the PUCO, and thus these operations are referred to herein as Duke Energy Ohio's regulated operations. Accordingly, beginning January 1, 2009, these revenues and corresponding fuel and purchased power expenses are recorded in Regulated Electric within Operating Revenues and Fuel Used in Electric Generation and Purchased Power—Regulated within Operating Expenses, respectively, on the Consolidated Statements of Operations.

Significant Risks and Uncertainties Associated with Customer Switching. Recently, surplus generating capacity caused by lower demand due to the economic recession has put downward pressure on power prices. The available capacity and lower prices have provided opportunities for customers in Ohio to switch generation suppliers. As a result, Duke Energy Ohio has experienced an increase in customer switching in the second quarter of 2009. In early August 2009, competitive power suppliers announced intentions of supplying power to current Duke Energy Ohio customers in Ohio at prices that are lower than Duke Energy Ohio's current ESP prices. While Duke Energy Ohio is unable to estimate the number of current customers who will switch to an alternative generation provider, which may include a retail sales affiliate of Cinergy, the impacts of customer switching could have a significant impact on the operations of Cinergy.

Furthermore, these evolving market conditions may potentially impact Cinergy's ability to continue to apply SFAS No. 71 to certain portions of Duke Energy Ohio's business. As of June 30, 2009, Duke Energy Ohio had regulatory assets of approximately \$200 million related to under-collections under the ESP and mark-to-market losses on certain economic hedges.

2. Acquisitions and Dispositions and Sales of Other Assets

Acquisitions. In June 2009, Cinergy acquired North Allegheny Wind, LLC (North Allegheny) in Western Pennsylvania for approximately \$124 million, of which approximately \$114 million was paid on the transaction date, with the remaining \$10 million paid in July 2009. The fair value of the assets acquired were determined primarily using a discounted cash flow model as the output of North Allegheny is contracted for 23 ½ years under a fixed price purchased power agreement. Substantially all of the fair value of the acquired net assets has been attributed to property, plant and equipment. There was no goodwill associated with this transaction. North Allegheny owns 70 MW of power generating assets that are expected to begin commercially generating electricity in the third quarter of 2009.

In June 2008, Cinergy announced the execution of a definitive agreement to acquire Catamount Energy Corporation (Catamount) from Diamond Castle Partners. Catamount is a leading wind power company located in Rutland, Vermont. The acquisition closed in September 2008 and expanded Cinergy's renewable energy portfolio to include over 300 MW of power generating assets, including 283 net MW in the Sweetwater wind power facility in West Texas, and 20 net MW of biomass-fueled cogeneration in New England. The acquisition also included approximately 1,750 MW of wind assets with the potential for development in the U.S. and United Kingdom. This transaction resulted in a purchase price of approximately \$245 million plus the assumption of approximately \$80 million of debt. The purchase accounting entries recorded upon acquisition primarily consisted of approximately \$190 million of equity method investments, approximately \$117 million of intangible assets related to wind development rights, approximately \$70 million of goodwill, none of which is deductible for tax purposes, and approximately \$80 million of debt.

Dispositions. In the first quarter of 2009, Cinergy completed the sale of two United Kingdom wind projects acquired in the Catamount acquisition. No gain or loss was recognized on these transactions. As these projects did not meet the definition of a disposal group as defined by SFAS No. 144, "Accounting for the Impairment or Disposal of Long-lived Assets" (SFAS No. 144), these projects were not reflected as held for sale on the Consolidated Balance Sheets prior to the completion of the sale.

Sales of Other Assets. For the three and six months ended June 30, 2009, the sale of other assets resulted in proceeds of approximately \$5 million and \$10 million, respectively, and net pre-tax gains of approximately \$1 million and \$5 million, respectively, recorded in Gains on Sales of Other Assets and Other, net on the Consolidated Statements of Operations. For the three and six months ended June 30, 2008, the sale of other assets resulted in proceeds of approximately \$44 million and \$63 million, respectively, and pre-tax gains of approximately \$33 million and \$49 million, respectively, recorded in Gains on Sales of Other Assets and Other, net on the Consolidated Statements of Operations. These amounts primarily relate to sales of emission allowances.

Notes to Unaudited Consolidated Financial Statements

3. Inventory

Inventory consists primarily of coal held for electric generation and materials and supplies and is recorded primarily using the average cost method. Inventory related to Cinergy's regulated operations is valued at historical cost consistent with ratemaking treatment. Materials and supplies are recorded as inventory when purchased and subsequently charged to expense or capitalized to plant when installed. Inventory related to Cinergy's non-regulated operations is valued at the lower of cost or market.

	June 30, 2009	December 31, 2008
	(in millions)	
Coal held for electric generation	\$ 313	\$ 238
Materials and supplies	162	164
Natural gas	3	3
Total inventory	\$ 478	\$ 405

Effective November 1, 2008, Duke Energy Ohio and Duke Energy Kentucky executed agreements with a third party to transfer title of natural gas inventory purchased by Duke Energy Ohio and Duke Energy Kentucky to the third party. Under the agreements, the gas inventory will be stored and managed for Duke Energy Ohio and Duke Energy Kentucky and will be delivered on demand. The gas storage agreements will expire on October 31, 2009, unless extended by the third party for an additional 12 months. As a result of the agreements, the combined natural gas inventory of approximately \$44 million and \$81 million being held by a third party as of June 30, 2009 and December 31, 2008, respectively, has been classified as Other within Current Assets on the Consolidated Balance Sheets.

4. Debt and Credit Facilities

First and Refunding Mortgage Bonds. In March 2009, Duke Energy Ohio issued \$450 million principal amount of first mortgage bonds, which carry a fixed interest rate of 5.45% and mature April 1, 2019. Proceeds from this issuance were used to repay short-term notes and for general corporate purposes, including funding capital expenditures.

In March 2009, Duke Energy Indiana issued \$450 million principal amount of first mortgage bonds, which carry a fixed interest rate of 6.45% and mature April 1, 2039. Proceeds from this issuance were used to fund capital expenditures, to replenish cash used to repay \$97 million of senior notes which matured on March 15, 2009, to fund the repayment at maturity of \$125 million of first mortgage bonds due July 15, 2009, and for general corporate purposes, including the repayment of short-term notes.

Other Debt. In June 2009, Duke Energy Indiana issued \$55 million of tax-exempt fixed rate term bonds, which are due August 1, 2039 and carry a fixed interest rate of 6.00%. The proceeds from this issuance were used to refund \$55 million of tax-exempt variable rate demand bonds on July 1, 2009.

In January 2009, Duke Energy Indiana refunded \$271 million of tax-exempt auction rate bonds through the issuance of \$271 million of tax-exempt variable-rate demand bonds, which are supported by direct-pay letters of credit, of which \$144 million had initial rates of 0.7% reset on a weekly basis with \$44 million maturing May 2035, \$23 million maturing March 2031 and \$77 million maturing December 2039. The remaining \$127 million had initial rates of 0.5% reset on a daily basis with \$77 million maturing December 2039 and \$50 million maturing October 2040.

Intercompany Loans and Money Pool. Cinergy receives support for a portion of its borrowing needs through intercompany loans from its parent entity, Duke Energy, and other Duke Energy subsidiaries, and its participation with Duke Energy and other Duke Energy subsidiaries in a money pool arrangement. Under the money pool arrangement, those companies with short-term funds may provide short-term loans to affiliates participating under this agreement. The money pool is structured such that Cinergy, Duke Energy Ohio, Duke Energy Indiana, and Duke Energy Kentucky separately manage their cash needs and working capital requirements. Accordingly there is no net settlement of receivables and payables of Cinergy, Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky, as each of these entities independently participate in the money pool.

As of June 30, 2009 and December 31, 2008, Cinergy had money pool receivables of approximately \$424 million and \$104 million, respectively, which are classified within Receivables in the accompanying Consolidated Balance Sheets. The \$320 million increase in receivables during the six months ended June 30, 2009 is reflected in Notes due from affiliate, net within Net cash used in investing activities on the Consolidated Statements of Cash Flows.

As of June 30, 2009, Cinergy had money pool borrowings of approximately \$184 million, of which approximately \$34 million is classified in Notes Payable within Current Liabilities and \$150 million is classified within Long-Term Debt in the accompanying Consolidated Balance Sheets. As of December 31, 2008, Cinergy had money pool borrowings of approximately \$196 million, of which approximately \$46 million is classified in Notes Payable within Current Liabilities and \$150 million is classified within Long-Term Debt in the accompanying Consolidated Balance Sheets. The \$12 million decrease in short-term money pool borrowings during the six months ended June 30, 2009 is reflected in Notes payable to affiliate, net within Net cash provided by (used in) financing activities on the Consolidated Statements of Cash Flows.

In addition, as of June 30, 2009 and December 31, 2008, Cinergy had intercompany loans outstanding with Duke Energy of approximately \$689 million, of which approximately \$659 million is classified in Notes Payable within Current Liabilities and approximately \$30 million is classified within Long-Term Debt in the accompanying Consolidated Balance Sheets, and approximately \$892 million, of which approximately \$868 million is classified in Notes Payable within Current Liabilities and approximately \$24 million is classified within Long-Term Debt in the accompanying Consolidated Balance Sheets, respectively. The \$203 million decrease in intercompany loans is reflected in Notes payable to affiliate, net within Net cash provided by (used in) financing activities on the Consolidated Statements of Cash Flows.

Available Credit Facilities and Capacity Utilized Under Available Credit Facilities. The total credit facility capacity under Duke Energy's master credit facility is approximately \$3.14 billion. Duke Energy has the unilateral ability under the master credit facility to increase or decrease the borrowing sub limits of each borrower, subject to maximum cap limitation, at any time. At June 30, 2009, Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky had borrowing sub limits under Duke Energy's master credit facility of \$650 million, \$450 million and \$100 million, respectively. The amount available to Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky under their sub limits to Duke Energy's master credit facility has been reduced by drawdowns of cash, borrowings through the money pool

Notes to Unaudited Consolidated Financial Statements

arrangement, and the use of the master credit facility to backstop issuances of letters of credit and pollution control bonds, as discussed below.

At June 30, 2009, Duke Energy and its wholly-owned subsidiaries, Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky (collectively referred to as the borrowers), had outstanding borrowings of approximately \$750 million under Duke Energy's master credit facility. Of the approximate \$750 million, Duke Energy Ohio's, Duke Energy Indiana's and Duke Energy Kentucky's portions are approximately \$279 million, \$123 million and \$74 million, respectively. The loans under the master credit facility are revolving credit loans that currently bear interest at one-month London Interbank Offered Rate (LIBOR) plus an applicable spread ranging from 19 to 24 basis points. The loans for the borrowers have stated maturities of September 2009; however, the borrowers have the ability under the master credit facility to renew the loans due in September 2009 up through the date the master credit facility matures, which is in June 2012. Except for Duke Energy Ohio, all of the borrowers have the intent and ability to refinance these obligations on a long-term basis, either through renewal of the terms of the loan through the master credit facility, which has non-cancelable terms in excess of one-year, or through issuance of long-term debt to replace the amounts drawn under the master credit facility. Accordingly, borrowings of approximately \$197 million are reflected as Long-Term Debt on the Consolidated Balance Sheets at both June 30, 2009 and December 31, 2008. Since Duke Energy Ohio does not have the intent to refinance these obligations on a long-term basis, Duke Energy Ohio's borrowing is reflected in Notes Payable within Current Liabilities on the Consolidated Balance Sheets at both June 30, 2009 and December 31, 2008. These borrowings reduce Duke Energy Ohio's, Duke Energy Indiana's and Duke Energy Kentucky's available credit capacity under Duke Energy's Master Credit Facility, as discussed above.

At June 30, 2009, approximately \$628 million of certain pollution control bonds and approximately \$180 million of intercompany loans between Cinergy and Duke Energy associated primarily with borrowings via the money pool, both of which are short-term obligations by nature, were classified as Long-Term Debt on the Consolidated Balance Sheets due to Cinergy's intent and ability to utilize such borrowings as long-term financing. Duke Energy's credit facilities with non-cancelable terms in excess of one year as of the balance sheet date give Cinergy the ability to refinance these short-term obligations on a long-term basis. Of the \$628 million of pollution control bonds outstanding at June 30, 2009, approximately \$245 million were backstopped by Duke Energy's master credit facility, with the remaining balance backstopped by other specific credit facilities separate from the master credit facility.

At December 31, 2008, approximately \$357 million of certain pollution control bonds were classified as Long-Term Debt on the Consolidated Balance Sheets for the reasons noted above.

Restrictive Debt Covenants. Duke Energy's debt and credit agreements contain various financial and other covenants. Cinergy's debt agreements also contain various financial and other covenants. Failure to meet these covenants beyond applicable grace periods could result in accelerated due dates and/or termination of the agreements. As of June 30, 2009, Duke Energy, Cinergy, Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky were in compliance with all covenants that would impact Cinergy's ability to borrow funds under the debt and credit facilities. In addition, some credit agreements may allow for acceleration of payments or termination of the agreements due to nonpayment, or the acceleration of other significant indebtedness of the borrower or some of its subsidiaries. None of the debt or credit agreements contain material adverse change clauses.

5. Employee Benefit Obligations

Net periodic benefit costs disclosed in the tables below for the qualified, non-qualified and other post-retirement benefit plans represent the cost of the respective benefit plan for the periods presented. However, portions of the net periodic benefit costs disclosed in the tables below have been capitalized as a component of property, plant and equipment.

Qualified Pension Plans

The following table shows the components of the net periodic pension costs for the Cinergy qualified pension plans.

Components of Net Periodic Pension Costs: Qualified Pension Costs

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009 ^(a)	2008 ^(a)	2009 ^(b)	2008 ^(b)
	(in millions)			
Service cost	\$ 8	\$ 10	\$ 17	\$ 19
Interest cost on projected benefit obligation	30	32	61	60
Expected return on plan assets	(38)	(35)	(78)	(69)
Amortization of prior service cost	2	2	3	3
Other	1	2	3	4
Net periodic pension costs	<u>\$ 3</u>	<u>\$ 11</u>	<u>\$ 6</u>	<u>\$ 17</u>

(a) Net periodic qualified pension costs for the three months ended June 30, 2009 and 2008 excludes approximately \$3 million and \$4 million, respectively, of regulatory asset amortization resulting from purchase accounting adjustments in connection with Cinergy's merger with Duke Energy in April 2006.

(b) Net periodic qualified pension costs for the six months ended June 30, 2009 and 2008 excludes approximately \$6 million and \$6 million, respectively, of regulatory asset amortization resulting from purchase accounting adjustments in connection with Cinergy's merger with Duke Energy in April 2006.

Notes to Unaudited Consolidated Financial Statements

Cinergy's policy is to fund amounts for its qualified pension plans on an actuarial basis to provide assets sufficient to meet benefit payments to be paid to plan participants. In February 2009, Cinergy made an approximate \$394 million contribution to the qualified pension plans. There were no contributions to the qualified pension plans during the six months ended June 30, 2008. Cinergy does not anticipate making additional contributions to its qualified or non-qualified pension plans during the remainder of 2009.

Non-Qualified Pension Plans

The following table shows the components of the net periodic pension costs for the Cinergy non-qualified pension plans.

Components of Net Periodic Pension Costs: Non-Qualified Pension Costs

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(in millions)			
Service cost	\$ —	\$ 1	\$ —	\$ 1
Interest cost on projected benefit obligation	1	1	3	3
Amortization of prior service cost	1	—	1	—
Amortization of loss	—	1	—	1
Net periodic pension costs	<u>\$ 2</u>	<u>\$ 3</u>	<u>\$ 4</u>	<u>\$ 5</u>

Other Post-Retirement Benefit Plans

The following table shows the components of the net periodic post-retirement benefit costs for the Cinergy other post-retirement benefit plans.

Components of Net Periodic Post-Retirement Benefit Costs

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009 ^(a)	2008 ^(a)	2009 ^(b)	2008 ^(b)
	(in millions)			
Service cost benefit	\$ 1	\$ 1	\$ 2	\$ 3
Interest cost on accumulated post-retirement benefit obligation	5	7	10	14
Expected return on plan assets	—	—	(1)	(1)
Amortization of prior service gain	(1)	—	(1)	—
Amortization of gain	(2)	—	(4)	—
Net periodic post-retirement benefit costs	<u>\$ 3</u>	<u>\$ 8</u>	<u>\$ 6</u>	<u>\$ 16</u>

- (a) Net periodic other post-retirement benefit costs for the three months ended June 30, 2009 and 2008 excludes approximately \$3 million and \$1 million, respectively, of regulatory asset amortization resulting from purchase accounting adjustments in connection with Cinergy's merger with Duke Energy in April 2006.
- (b) Net periodic other post-retirement benefit costs for the six months ended June 30, 2009 and 2008 excludes approximately \$5 million and \$3 million, respectively, of regulatory asset amortization resulting from purchase accounting adjustments in connection with Cinergy's merger with Duke Energy in April 2006.

Employee Savings Plans

Cinergy also sponsors employee savings plans that cover substantially all employees. Cinergy expensed pre-tax employer matching contributions of approximately \$2 million and \$6 million during the three and six months ended June 30, 2009, respectively. Cinergy expensed pre-tax employer matching contributions of approximately \$6 million and \$14 million during the three and six months ended June 30, 2008, respectively.

Notes to Unaudited Consolidated Financial Statements

6. Goodwill and Intangibles

Carrying Amount of Goodwill

Cinergy evaluates the carrying amount of its recorded goodwill for impairment under the guidance of SFAS No. 142, "Goodwill and Intangible Assets." As required under GAAP in the U.S., Cinergy performs an annual goodwill impairment test and updates the test between annual tests if events or circumstances occur that would more likely than not reduce the fair value of a reporting unit below its carrying amount. Cinergy performs its annual impairment assessment as of August 31 each year. As of the date of the August 2008 annual impairment test, the fair value of Cinergy's reporting units exceeded their respective carrying values, thus no goodwill impairment charges were recorded. Subsequent to the August 2008 annual impairment test, management has continued to monitor the impact of market and economic events to determine if it is more likely than not that the carrying values of Cinergy's reporting units have been impaired. As of June 30, 2009, management evaluated all significant triggering events or circumstances that existed as of that date and concluded that it was not more likely than not that the fair value of a reporting unit was below its carrying value, and therefore, management did not perform an interim detailed impairment test of Cinergy's goodwill. Subsequent to June 30, 2009, as discussed further in Note 1, market conditions impacting Duke Energy Ohio continue to rapidly evolve and it is possible that goodwill impairment charges could be recorded in the future as a result of the changing business environment. At June 30, 2009 and December 31, 2008, Cinergy had total goodwill of approximately \$4,459 million and \$4,460 million, respectively.

Intangible Assets

The carrying amount and accumulated amortization of intangible assets as of June 30, 2009 and December 31, 2008 are as follows:

	<u>June 30, 2009</u>	<u>December 31, 2008</u>
(in millions)		
Emission allowances	\$ 284	\$ 298
Gas, coal and power contracts	295	295
Wind development rights ^(a)	127	161
Other	10	12
Total gross carrying amount	<u>716</u>	<u>766</u>
Accumulated amortization—gas, coal and power contracts	(129)	(117)
Accumulated amortization—other	(8)	(10)
Total accumulated amortization	<u>(137)</u>	<u>(127)</u>
Total intangible assets, net	<u>\$ 579</u>	<u>\$ 639</u>

- (a) As discussed further below and in Note 2, the decrease in wind development rights primarily relates to the sale of certain projects that were acquired as part of Catamount in September 2008.

Emission allowances in the table above include emission allowances which were recorded at the then fair value on the date of Cinergy's merger with Duke Energy in April 2006, and emission allowances purchased by Cinergy. Additionally, Cinergy is allocated certain zero cost emission allowances on an annual basis. The change in the gross carrying value of emission allowances during the six months ended June 30, 2009 is as follows:

	(in millions)
Gross carrying value at beginning of period	\$ 298
Purchases of emission allowances	38
Sales and consumption of emission allowances ^{(a)(b)}	(54)
Other changes	2
Gross carrying value at end of period	<u>\$ 284</u>

- (a) Carrying value of emission allowances are recognized via a charge to expense when consumed. Carrying value of emission allowances sold or consumed during the six months ended June 30, 2008 was approximately \$65 million.
- (b) See Note 2 for a discussion of gains on sales of emission allowances during the six months ended June 30, 2009 and 2008.

Amortization expense for gas, coal and power contracts and other intangible assets was approximately \$4 million and \$6 million for the three months ended June 30, 2009 and 2008, respectively, and approximately \$10 million and \$13 million for the six months ended June 30, 2009 and 2008, respectively.

As discussed in Note 2, Cinergy completed the acquisition of Catamount in September 2008, resulting in the recognition of approximately \$117 million of intangible assets related to wind farm development rights. Of this amount, a portion of the intangible asset value was assigned to projects that Cinergy disposed of through sale in the first quarter of 2009. The intangible assets recorded in connection with the Catamount acquisition primarily represent land use rights and interconnection agreements acquired by Cinergy as part of the purchase price. Since these intangible assets relate to development projects for which commercial operations have not commenced, amortization of the intangible asset value assigned to each of these projects will not begin until commercial operation is achieved. Cinergy will evaluate the useful lives of these intangible assets as the projects begin commercial operations, which is anticipated to be in the years 2010 through 2012. Cinergy currently estimates the useful lives of these projects, once in commercial operation, will be the shorter of the lease term of the land or the estimated lives of the projects, which is approximately 25 years.

Notes to Unaudited Consolidated Financial Statements

Intangible Liabilities

In connection with the merger with Duke Energy in April 2006, Cinergy recorded an intangible liability of approximately \$113 million associated with the RSP in Ohio, which was recognized in earnings over the regulatory period that ended on December 31, 2008. This liability became fully amortized in the fourth quarter of 2008. Cinergy also recorded approximately \$56 million of intangible liabilities associated with other power sale contracts in connection with the merger with Duke Energy. The carrying amount of these intangible liabilities associated with other power sale contracts was approximately \$13 million and \$16 million at June 30, 2009 and December 31, 2008, respectively. During the three and six months ended June 30, 2009, Cinergy amortized approximately \$2 million and \$3 million, respectively, to income related to these intangible liabilities. During the three and six months ended June 30, 2008, Cinergy amortized approximately \$18 million and \$36 million, respectively, to income related to these intangible liabilities. Intangible liabilities are classified as Other within Deferred Credits and Other Liabilities on the Consolidated Balance Sheets.

7. Discontinued Operations and Assets Held for Sale

Income From Discontinued Operations, net of tax was insignificant for the three and six months ended June 30, 2009 and approximately \$16 million and \$24 million for the three and six months ended June 30, 2008, respectively. There were no Assets Held for Sale and Liabilities Associated with Assets Held for Sale in the Consolidated Balance Sheets as of June 30, 2009 or December 31, 2008.

The income recorded during the three and six months ended June 30, 2008 primarily relates to Cinergy's gain on the sale of its 480 MW natural gas-fired peaking generation station located near Brownsville, Tennessee to Tennessee Valley Authority for approximately \$55 million in April 2008. This transaction resulted in Cinergy recognizing an approximate \$23 million pre-tax gain at closing.

8. Related Party Transactions

Cinergy engages in related party transactions, which are generally performed at cost and in accordance with the applicable state and federal commission regulations. Balances due to or due from related parties included in the Consolidated Balance Sheets as of June 30, 2009 and December 31, 2008 are as follows:

	June 30, 2009^(a)	December 31, 2008^(a)
(in millions)		
Current assets ^(b)	\$ 219	\$ 203
Current liabilities ^(c)	\$ (95)	\$ (18)
Net deferred tax liabilities ^(d)	\$ (2,305)	\$ (2,052)

- (a) Balances exclude assets or liabilities associated with Cinergy Receivables and money pool arrangements as discussed below.
- (b) Of the balance at June 30, 2009, approximately \$25 million is classified as Receivables and approximately \$194 million is classified as Other within Current Assets on the Consolidated Balance Sheets. Of the balance at December 31, 2008, approximately \$172 million is classified as Receivables and approximately \$31 million is classified as Other within Current Assets on the Consolidated Balance Sheets.
- (c) The balances at June 30, 2009 and December 31, 2008 are classified as Accounts payable on the Consolidated Balance Sheets.
- (d) Of the balance at June 30, 2009, approximately \$(2,338) million is classified as Deferred income taxes and approximately \$33 million is classified as Other within Current Assets on the Consolidated Balance Sheets. Of the balance at December 31, 2008, approximately \$(2,145) million is classified as Deferred income taxes and approximately \$93 million is classified as Other within Current Assets on the Consolidated Balance Sheets.

Cinergy is allocated its proportionate share of corporate governance and other costs by an unconsolidated affiliate that is a consolidated affiliate of Duke Energy. Additionally, prior to July 1, 2008, Duke Energy and its subsidiaries were allocated their proportionate share of corporate governance costs from a consolidated affiliate of Cinergy. Corporate governance and other shared services costs are primarily allocations of corporate costs, such as human resources, legal and accounting fees, as well as other third party costs. During the three months ended June 30, 2009 and 2008, Cinergy recorded governance and shared services expenses of approximately \$244 million and \$259 million, respectively, which are recorded in Operation, Maintenance and Other within Operating Expenses on the Consolidated Statements of Operations. During the six months ended June 30, 2009 and 2008, Cinergy recorded governance and shared services expenses of approximately \$484 million and \$499 million, respectively, which are recorded in Operation, Maintenance and Other within Operating Expenses on the Consolidated Statements of Operations.

Prior to July 1, 2008, Cinergy also recognized recoveries of direct and allocated corporate governance and shared service costs charged to affiliates. These recoveries were primarily reflected as an offset within Operating Expense on the Consolidated Statements of Operations and were approximately \$24 million and \$51 million for the three and six months ended June 30, 2008.

Cinergy incurs expenses related to certain insurance coverages through Bison Insurance Company Limited, Duke Energy's wholly-owned captive insurance subsidiary. These expenses, which are recorded in Operation, Maintenance and Other within Operating Expenses on the Consolidated Statements of Operations, were approximately \$6 million for each of the three months ended June 30, 2009 and 2008, and approximately \$13 million for each of the six months ended June 30, 2009 and 2008. Cinergy records income associated with the rental of office space to a consolidated affiliate of Duke Energy. Rental income was approximately \$5 million and \$10 million for the three and six months ended June 30, 2009. There was no rental income for the three or six months ended June 30, 2008.

As discussed in Notes 1 and 17, certain trade receivables have been sold by Cinergy to Cinergy Receivables. The proceeds obtained from the sales of receivables are largely cash but do include a subordinated note from Cinergy Receivables for a portion of the purchase price. This subordinated note is classified as Receivables in the Consolidated Balance Sheets and was approximately \$286 million and \$292 million as of June 30, 2009 and December 31, 2008, respectively. The interest income associated with the subordinated note, which is recorded in Other Income and Expenses, net on the Consolidated Statements of Operations, was approximately \$6 million and \$8 million for the three months ended June 30, 2009 and 2008, respectively, and approximately \$14 million and \$20 million for the six months ended June 30, 2009 and 2008, respectively.

As discussed further in Note 4, Cinergy participates in a money pool arrangement with its parent entity, Duke Energy, and other Duke Energy subsidiaries, and receives support for its short-term borrowing needs through intercompany loans from Duke Energy. The expenses associated with this activity, which are recorded in Interest Expense on the Consolidated Statements of Operations, were approximately \$2

Notes to Unaudited Consolidated Financial Statements

million for each of the three months ended June 30, 2009 and 2008, and approximately \$6 million and \$7 million for the six months ended June 30, 2009 and 2008, respectively.

9. Risk Management, Derivative Instruments and Hedging Activities

The primary risks Cinergy manages by utilizing derivative instruments are commodity price risk and interest rate risk. Cinergy closely monitors the risks associated with commodity price changes and changes in interest rates on its operations and, where appropriate, uses various commodity and interest rate instruments to manage these risks. Certain of these derivative instruments are designated as hedging instruments under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS No. 133), while others either do not qualify as a hedge or have not been designated as hedges by Cinergy (hereinafter referred to as undesignated contracts). Cinergy's primary use of energy commodity derivatives is to hedge its generation portfolio against exposure to the prices of power and fuel. Interest rate swaps are entered into to manage interest rate risk primarily associated with Cinergy's variable-rate and fixed-rate borrowings.

SFAS No. 133 requires the recognition of all derivative instruments as either assets or liabilities at fair value in the Consolidated Balance Sheets. In accordance with SFAS No. 133, Cinergy may elect to designate qualifying commodity and interest rate derivatives as either cash flow hedges or fair value hedges.

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss is reported as a component of Accumulated Other Comprehensive Income (AOCI) and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Any gains or losses on the derivative that represent either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings. For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative as well as the offsetting loss or gain on the hedged item are recognized in earnings in the current period. Cinergy includes the gain or loss on the hedged items in the same line item as the offsetting loss or gain on the derivative in the Consolidated Statements of Operations. Additionally, Cinergy enters into derivative agreements that are economic hedges that either do not qualify for hedge accounting or have not been designated as a hedge. These derivative instruments are typically reflected on the Consolidated Balance Sheets at fair value with changes in the value of the derivative instrument reflected in regulatory assets or liabilities, as discussed below, or possibly in current earnings.

As Cinergy's regulated operations apply the provisions of SFAS No. 71, certain gains and losses associated with undesignated contracts are deferred as regulatory liabilities and assets, respectively, thus there is no immediate earnings impact associated with the change in fair values associated with these derivative contracts.

Commodity Price Risk

Cinergy is exposed to the impact of market changes in the future prices of electricity (energy, capacity and financial transmission rights), coal, natural gas and emission allowances (sulfur dioxide (SO₂), seasonal nitrogen oxide (NO_x) and annual NO_x) as a result of its energy operations such as electric generation and natural gas distribution. With respect to commodity price risks associated with electric generation, Cinergy is exposed to changes including, but not limited to, the cost of coal and natural gas used to generate electricity, the prices of electricity in wholesale markets, the cost of capacity required to purchase and sell electricity in wholesale markets and the cost of emission allowances for SO₂, seasonal NO_x and annual NO_x, primarily at Cinergy's coal fired power plants. Cinergy closely monitors the risks associated with commodity price changes on its future operations and, where appropriate, uses various commodity contracts to mitigate the effect of such fluctuations on operations. Cinergy's exposure to commodity price risk is influenced by a number of factors, including, but not limited to, the term of the contract, the liquidity of the market and delivery location.

Commodity derivatives associated with the risk management of Cinergy's energy operations are accounted for as either cash flow hedges or fair value hedges if the derivative instrument qualifies as a hedge under SFAS No. 133, or as an undesignated contract if either the derivative instrument does not qualify as a hedge or Cinergy has elected to not designate the contract as a hedge. Additionally, Cinergy enters into various contracts that qualify for the normal purchase and normal sales (NPNS) exception described in paragraph 10 of SFAS No. 133, as amended. Cinergy primarily applies the NPNS exception to contracts that relate to the physical delivery of electricity over the next 12 years.

Commodity Fair Value Hedges. At June 30, 2009, Cinergy did not have any open commodity derivative instruments that were designated as fair value hedges under SFAS No. 133.

Commodity Cash Flow Hedges. Cinergy uses commodity instruments, such as swaps, futures, forwards and options, to protect margins for a portion of future revenues and fuel and purchased power expenses. Cinergy generally uses commodity cash flow hedges to mitigate exposures to the price variability of the underlying commodities for a maximum period of 1 year.

Undesignated Contracts. Cinergy uses derivative contracts as economic hedges to manage the market risk exposures that arise from providing electric generation and capacity to large energy customers, energy aggregators and other wholesale companies. Undesignated contracts include contracts not designated as a hedge, contracts that do not qualify for hedge accounting, derivatives that no longer qualify for the NPNS scope exception, and de-designated hedge contracts that were not re-designated as a hedge. The contracts in this category as of June 30, 2009 are primarily associated with forward power sales and coal purchases, as well as forward SO₂ emission allowances.

Interest Rate Risk

Cinergy is exposed to risk resulting from changes in interest rates as a result of its issuance or anticipated issuance of variable and fixed-rate debt and commercial paper. Cinergy manages its interest rate exposure by limiting its variable-rate exposures to a percentage of total capitalization and by monitoring the effects of market changes in interest rates. To manage risk associated with changes in interest rates, Cinergy may enter into financial contracts, primarily interest rate swaps and U.S. Treasury lock agreements. All of Cinergy's derivative instruments related to interest rate risk are categorized as undesignated contracts. At June 30, 2009, the total notional amount of Cinergy's receive variable/pay-fixed interest rate swaps was approximately \$76 million.

Volumes

The following table shows information relating to the volume of Cinergy's derivative activity as of June 30, 2009. Amounts disclosed represent the notional volumes of commodities and the notional dollar amounts of debt subject to derivative contracts accounted for at fair value in accordance with SFAS No. 133. For option contracts, notional amounts include only the delta-equivalent volumes which represent the notional volumes times the probability of exercising the option based on current price volatility. Volumes associated with contracts qualifying for the NPNS exception have been excluded from the table below. Amounts disclosed represent the absolute value of notional amounts. Cinergy has netted contractual amounts where offsetting purchase and sale contracts exist with identical delivery locations and times of delivery.

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Underlying Notional Amounts for Derivative Instruments Accounted for At Fair Value

	June 30, 2009
<u>Commodity contracts</u>	
Electricity-energy (Gigawatt hours)	2,705
Emission allowances: SO ₂ (thousands of tons)	91
Emission allowances: NO _x (thousands of tons)	3
Natural gas (millions of decatherms)	8
Coal (millions of tons)	4
<u>Financial contracts</u>	
Interest rates (dollars in millions)	\$ 76

The following table shows fair value amounts of derivative contracts as of June 30, 2009 and the line item(s) in the Consolidated Balance Sheets in which such amounts are included. The fair values of derivative contracts are presented on a gross basis, even when the derivative instruments are subject to master netting arrangements. Cash collateral payables and receivables associated with the derivative contracts have not been netted against the fair value amounts.

Location and Fair Value Amounts of Derivatives reflected in the Consolidated Balance Sheets

	June 30, 2009	
<u>Balance Sheet Location</u>	<u>Asset</u> <u>Derivatives</u>	<u>Liability</u> <u>Derivatives</u>
	(in millions)	
Derivatives Designated as Hedging Instruments Under SFAS No. 133		
<u>Commodity contracts</u>		
Investments and Other Assets: Other	\$ 1	\$ -
Total Derivatives Designated as Hedging Instruments Under SFAS No. 133	\$ 1	\$ -
Derivatives Not Designated as Hedging Instruments Under SFAS No. 133		
<u>Commodity contracts</u>		
Current Assets: Other	\$ 71	\$ 13
Investments and Other Assets: Other	63	13
Current Liabilities: Other	174	326
Deferred Credits and Other Liabilities: Other	39	151
<u>Interest rate contracts</u>		
Current Liabilities: Other	-	3
Deferred Credits and Other Liabilities: Other	-	5
Total Derivatives Not Designated as Hedging Instruments Under SFAS No. 133	\$347	\$511
Total Derivatives	\$348	\$511

The following table shows the amount of the losses recognized on derivative instruments designated and qualifying as cash flow hedges by type of derivative contract during the three and six months ended June 30, 2009 and the financial statement line items in which such losses are included.

Cash Flow Hedges – Location and Amount of Pre-tax Losses Recognized in Comprehensive Income

	Three Months Ended Six Months Ended	
	June 30, 2009	June 30, 2009
	(in millions)	
Location of Pre-tax Losses Reclassified from AOCI into Earnings^(a)		
<u>Commodity contracts</u>		
Revenue, non-regulated electric and other	\$ (5)	\$(12)
Fuel used in electric generation and purchased power-non-regulated	(1)	(7)
Total Pre-tax Losses Reclassified from AOCI into Earnings	\$ (6)	\$(19)

(a) Represents the gains and losses on cash flow hedges previously recorded in AOCI during the term of the hedging relationship and reclassified into earnings during the current period.

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The effective portion of gains or losses on cash flow hedges that were recognized in AOCI during the three and six months ended June 30, 2009 were insignificant. In addition, there was no hedge ineffectiveness during the six months ended June 30, 2009. No gains or losses have been excluded from the assessment of hedge effectiveness. As of June 30, 2009, approximately \$2 million of pre-tax deferred net losses on derivative instruments related to commodity cash flow hedges and interest rate hedges are accumulated on the Consolidated Balance Sheets in AOCI are expected to be recognized in earnings during the next twelve months as the hedged transactions occur.

The following table shows the amount of the pre-tax gains and losses recognized on undesignated hedges by type of derivative instrument during the three and six months ended June 30, 2009 and the line item(s) in the Consolidated Statements of Operations in which such gains and losses are included or deferred on the Consolidated Balance Sheets as regulatory assets.

Undesignated Hedges – Location and Amount of Pre-tax Gains and (Losses) Recognized in Income or as Regulatory Assets

	Three Months Ended	Six Months Ended
	June 30, 2009	June 30, 2009
(in millions)		
Location of Pre-tax Gains and (Losses) Recognized in Earnings		
<u>Commodity contracts</u>		
Revenue, non-regulated electric and other	\$ (17)	\$ 4
Fuel used in electric generation and purchased power-non-regulated	(16)	(24)
<u>Interest rate contracts</u>		
Interest expense	<u>1</u>	<u>-</u>
Total Pre-tax Losses Recognized in Earnings	<u>\$ (32)</u>	<u>\$ (20)</u>
Location of Pre-tax Gains and (Losses) Recognized as Regulatory Assets		
<u>Commodity contracts</u>		
Regulatory Asset	\$ 42	\$ (37)
<u>Interest rate contracts</u>		
Regulatory Asset	<u>2</u>	<u>-</u>
Total Pre-tax Gains (Losses) Recognized as Regulatory Assets	<u>\$ 44</u>	<u>\$ (37)</u>

Certain of Cinergy's derivative contracts contain contingent credit features, such as material adverse change clauses or payment acceleration clauses that could result in immediate payments, the posting of letters of credit or the termination of the derivative contract before maturity if specific events occur, such as a downgrade of Cinergy's credit rating below investment grade.

The following table shows information with respect to derivative contracts that are in a net liability position and contain objective credit-risk related payment provisions. The amounts disclosed in the table below represents the aggregate fair value amounts of such derivative instruments at the end of the reporting period, the aggregate fair value of assets that are already posted as collateral under such derivative instruments at the end of the reporting period, and the aggregate fair value of additional assets that would be required to be transferred in the event that credit-risk-related contingent features were triggered at June 30, 2009.

Information Regarding Derivative Instruments that Contain Credit-risk Related Contingent Features

	June 30, 2009
(in millions)	
Aggregate Fair Value Amounts of Derivative Instruments in a Net Liability Position	\$ 386
Collateral Already Posted	\$ 193
Additional Cash Collateral or Letters of Credit in the Event Credit-risk-related Contingent Features were Triggered at the End of the Reporting Period	\$ 20

Netting of cash collateral and derivative assets and liabilities under master netting arrangements. In accordance with FASB Staff Position (FSP) No. FIN 39-1, "Amendment of FASB Interpretation No 39, Offsetting of Amounts Related to Certain Contracts" (FSP No. FIN 39-1), Cinergy offsets fair value amounts (or amounts that approximate fair value) recognized on its Consolidated Balance Sheets related to cash collateral amounts receivable or payable against fair value amounts recognized for derivative instruments executed with the same counterparty under the same master netting agreement. At June 30, 2009 and December 31, 2008, Cinergy had receivables related to the right to reclaim cash collateral of approximately \$148 million and \$86 million, respectively, and had payables related to obligations to return cash collateral of insignificant amounts, respectively, that have been offset against net derivative positions in the Consolidated Balance Sheets. Cinergy had \$46 million and approximately \$64 million in cash collateral receivables under master netting arrangements that have not been offset against net derivative positions at June 30, 2009 and December 31, 2008, respectively, as these amounts primarily represent initial margin deposits related to New York Mercantile Exchange (NYMEX) futures contracts. Cinergy had insignificant cash collateral payables under master netting arrangements that have not been offset against net derivative positions at June 30, 2009 and December 31, 2008.

See Note 13 for additional information on fair value disclosures related to derivatives required by SFAS No. 157, "Fair Value Measurements" (SFAS No. 157).

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10. Regulatory Matters

Rate Related Information. The Indiana Utility Regulatory Commission (IURC) and Kentucky Public Service Commission (KPSC) approve rates for retail electric and gas services within their states. The PUCO approves rates and market prices for retail gas and electric service within the state of Ohio, except that non-regulated sellers of gas and electric generation also are allowed to operate in Ohio. The Federal Energy Regulatory Commission (FERC) approves rates for electric sales to wholesale customers served under cost-based rates.

Duke Energy Ohio Electric Rate Filings. New legislation (SB 221) codifies the PUCO's authority to approve an electric utility's standard service offer through an ESP, which would allow for pricing structures similar to those under the historic RSP. Electric utilities are required to file an ESP and may also file an application for a MRO at the same time. The MRO is a price determined through a competitive bidding process. SB 221 provides for the PUCO to approve non-by-passable charges for new generation, including construction work-in-process from the outset of construction, as part of an ESP. The new law grants the PUCO discretion to approve single issue rate adjustments to distribution and transmission rates and establishes new alternative energy resources (including renewable energy) portfolio standards, such that a utility's portfolio must consist of at least 25% of these resources by 2025. SB 221 also provides a separate requirement for energy efficiency, which must reduce a utility's load by 22% before 2025. A utility's earnings under the ESP is subject to an annual earnings test and the PUCO must order a refund if it finds that the utility's earnings significantly exceed the earnings of benchmark companies with similar business and financial risks. The earnings test acts as a cap to the ESP price. SB 221 also limits the ability of a utility to transfer its designated generating assets to an exempt wholesale generator (EWG) absent PUCO approval.

On July 31, 2008, Duke Energy Ohio filed an ESP to be effective January 1, 2009.

On December 17, 2008, the PUCO issued its finding and order adopting a modified Stipulation with respect to Duke Energy Ohio's ESP filing. The PUCO agreed to Duke Energy Ohio's request for a net increase in base generation revenues of \$36 million, \$74 million and \$98 million in 2009, 2010 and 2011, respectively, including the termination of the residential and non-residential RTC, the recovery of expenditures incurred to deploy the SmartGrid infrastructure and the implementation of save-a-watt. The Stipulation also allowed Duke Energy Ohio to defer up to \$50 million of certain operation and maintenance costs incurred at the W.C. Beckjord generating station and to amortize those costs over the three-year ESP period. The PUCO modified the Stipulation to permit certain non-residential customers to opt out of utility-sponsored energy efficiency initiatives and to allow residential governmental aggregation customers who leave Duke Energy Ohio's system to avoid some charges. Applications for rehearing of the PUCO's decision were filed by environmental groups and a residential customer advocate group. On February 11, 2009, the PUCO issued an Entry denying the rehearing requests. On April 13, 2009, the Office of the Ohio Consumers' Counsel (OCC) filed a notice of appeal to the Ohio Supreme Court, challenging the PUCO's interpretation of the system-reliability-adjustment capacity dedication rider (SRA-CD). The OCC claims that the PUCO incorrectly determined that SRA-CD is unavoidable for residential governmental aggregation customers. Duke Energy Ohio was granted leave to intervene as an appellee in the proceeding. The OCC has filed its merit brief, and amicus briefs in support of the OCC's position were filed by Direct Energy Services, LLC and the Northeast Ohio Public Energy Council. Appellees' merit briefs are due on September 1, 2009.

As discussed in Note 1, as a result of the approval of the ESP, effective December 17, 2008, Duke Energy Ohio reapplied SFAS No. 71 to certain portions of its operations.

Duke Energy Ohio Gas Rate Case. In July 2007, Duke Energy Ohio filed an application with the PUCO for an increase in its base rates for gas service. Duke Energy Ohio sought an increase of approximately \$34 million in revenue, or approximately 5.7%, to be effective in the spring of 2008. The application also requested approval to continue tracker recovery of costs associated with the accelerated gas main replacement program. On February 28, 2008, Duke Energy Ohio reached a settlement agreement with the PUCO Staff and all of the intervening parties on its request for an increase in natural gas base rates. The settlement called for an annual revenue increase of approximately \$18 million in base revenue, or 3% over current revenue, permitted continued recovery of costs through 2018 for Duke Energy Ohio's accelerated gas main replacement program and permitted recovery of carrying costs on gas stored underground via its monthly gas cost adjustment filing. The settlement did not resolve a proposed rate design for residential customers, which involved moving more of the fixed charges of providing gas service, such as capital investment in pipes and regulating equipment, billing and meter reading, from the per unit charges to the monthly charge. On May 28, 2008, the PUCO approved the settlement in its entirety and the proposed rate design. On June 28, 2008, the OCC and Ohio Partners for Affordable Energy (OPAЕ) filed Applications for Rehearing opposing the rate design. On July 23, 2008, the PUCO issued an Entry denying the rehearing requests of OCC and OPAЕ. On September 16 and 19, 2008, the OCC and OPAЕ, respectively, filed their notices of appeal to the Ohio Supreme Court opposing the residential rate design issue. Merit briefs were filed with the Ohio Supreme Court on February 2, 2009. On April 10, 2009, the OCC provided statutory notice of its intent to seek a stay of the implementation of State 3 of the approved rate design. On June 1, 2009, the Ohio Supreme Court denied the OCC's motion to stay. As a result, Stage 3 of the straight fixed variable rate design was implemented effective June 1, 2009. On July 7, 2009, the Ohio Supreme Court scheduled oral argument for September 16, 2009. At this time, Duke Energy Ohio cannot predict whether the Ohio Supreme Court will reverse the PUCO's decision of May 28, 2008.

Duke Energy Ohio Electric Distribution Rate Case. On June 25, 2008, Duke Energy Ohio filed notice with the PUCO that it would seek a rate increase for electric delivery service of approximately \$86 million, or 4.8% of total electric revenues, to be effective in the second quarter of 2009. On December 22, 2008, Duke Energy Ohio filed an application requesting deferral of approximately \$31 million related to damage to its distribution system from a September 14, 2008 windstorm, which was granted by the PUCO. Accordingly, a regulatory asset was recorded as of December 31, 2008 for \$31 million. On March 31, 2009, Duke Energy Ohio and Parties to the case filed a Stipulation and Recommendation which settles all issues in the case. The Stipulation provided for a revenue increase of \$55.3 million, or approximately a 2.9% overall increase. The Parties also agreed that Duke Energy Ohio will recover any approved costs associated with the September 14, 2008 wind storm restoration through a separate rider recovery mechanism. Duke Energy Ohio agreed to file a separate application to set the rider and the PUCO will review the request and determine the appropriate amount of storm costs that should be recovered. The Stipulation includes, among other things, a weatherization and energy efficiency program, and recovery of distribution-related bad debt expenses through a rider mechanism. The Stipulation was approved in its entirety by the PUCO on July 8, 2009. An application for rehearing was filed on July 21, 2009 and Duke Energy Ohio filed a memorandum in opposition on July 31, 2009. On August 12, 2009, the PUCO denied the Application for Rehearing.

Duke Energy Kentucky Gas Rate Cases. In 2002, the KPSC approved Duke Energy Kentucky's gas base rate case which included, among other things, recovery of costs associated with an accelerated gas main replacement program. The approval authorized a tracking mechanism to recover certain costs including depreciation and a rate of return on the program's capital expenditures. The Kentucky Attorney General appealed to the Franklin Circuit Court the KPSC's approval of the tracking mechanism as well as the KPSC's subsequent approval of annual rate adjustments under this tracking mechanism. In 2005, both Duke Energy Kentucky and the KPSC requested that the court dismiss these cases.

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In February 2005, Duke Energy Kentucky filed a gas base rate case with the KPSC requesting approval to continue the tracking mechanism and for a \$14 million annual increase in base rates. A portion of the increase was attributable to recovery of the current cost of the accelerated gas main replacement program in base rates. In June 2005, the Kentucky General Assembly enacted Kentucky Revised Statute 278.509 (KRS 278.509), which specifically authorizes the KPSC to approve tracker recovery for utilities' gas main replacement programs. In December 2005, the KPSC approved an annual rate increase of \$8 million and re-approved the tracking mechanism through 2011. In February 2006, the Kentucky Attorney General appealed the KPSC's order to the Franklin Circuit Court, claiming that the order improperly allows Duke Energy Kentucky to increase its rates for gas main replacement costs in between general rate cases, and also claiming that the order improperly allows Duke Energy Kentucky to earn a return on investment for the costs recovered under the tracking mechanism which permits Duke Energy Kentucky to recover its gas main replacement costs.

In August 2007, the Franklin Circuit Court consolidated all the pending appeals and ruled that the KPSC lacks legal authority to approve the gas main replacement tracking mechanism, which were approved prior to enactment of KRS 278.509. To date, Duke Energy Kentucky has collected approximately \$9 million in annual rate adjustments under the tracking mechanism. Per the KPSC order, Duke Energy Kentucky collected these revenues subject to refund pending the final outcome of this litigation. Duke Energy Kentucky and the KPSC have requested that the Kentucky Court of Appeals grant a rehearing of its decision. On February 5, 2009, the Kentucky Court of Appeals denied the rehearing requests of both Duke Energy Kentucky and the KPSC. Duke Energy Kentucky filed a motion for discretionary review to the Kentucky Supreme Court on March 9, 2009. On August 25, 2009, the Kentucky Supreme Court accepted Duke Energy Kentucky's request for review. A date for the hearing has not yet been set.

On July 1, 2009, Duke Energy Kentucky filed its application for an increase of approximately \$17.5 million in base natural gas rates. Duke Energy Kentucky also proposed to implement a new rate design for residential customers, which involves moving more of the fixed charges of providing gas service, such as capital investment in pipes and regulating equipment, billing and meter reading, from the per unit charges to the monthly charge. The application is pending and at this time, Duke Energy Kentucky cannot predict the outcome of this proceeding. A procedural schedule excluding a hearing date was issued on July 31, 2009. Intervenor testimony is due on October 12, 2009. Discovery from intervenors must be completed by November 9, 2009. Duke Energy Kentucky must file rebuttal testimony by November 23, 2009.

Indiana Allowance For Funds Used During Construction (AFUDC) Ruling. Duke Energy Indiana recovers financing and other operating costs associated with certain environmental control property through a rate adjustment mechanism. In January 2008, the IURC approved the inclusion of an accounting adjustment for AFUDC affecting the value of the property. The Indiana Office of Utility Consumer Counselor (OUCC) filed a petition asking the IURC to rehear and reconsider its decision regarding approval of the amount of AFUDC included in the value of the property. The IURC issued an order in the second quarter of 2008 denying the OUCC's request and upholding its original decision. The OUCC appealed the IURC's Order on Reconsideration to the Indiana Court of Appeals. On November 14, 2008, the Indiana Court of Appeals affirmed the IURC order approving the accounting adjustment for AFUDC. Duke Energy Indiana recorded the favorable impacts of this IURC ruling as a component of Other Income and Expenses, net on the Consolidated Statements of Operations, which amounted to approximately \$25 million during the six months ended June 30, 2008, of which approximately \$18 million was recorded during the three months ended June 30, 2008.

Duke Energy Ohio Energy Efficiency. On July 11, 2007, the PUCO approved Duke Energy Ohio's Demand Side Management/Energy Efficiency Program (DSM Program). The DSM programs were first proposed in 2006 and were endorsed by the Duke Energy Community Partnership, which is a collaborative group made up of representatives of organizations interested in energy conservation, efficiency and assistance to low-income customers. The program costs are recouped through a cost recovery mechanism that will be adjusted annually to reflect the previous year's activity. Duke Energy Ohio is permitted to recover lost revenues, program costs and shared savings (once the programs reach 65% of the targeted savings level) through the cost recovery mechanism based upon impact studies to be provided to the Staff of the PUCO. Duke Energy Ohio filed the save-a-watt Energy Efficiency Plan as part of its ESP filed with the PUCO on July 31, 2008 (discussed above). On December 17, 2008, the PUCO approved the ESP, including allowing for the implementation of a new save-a-watt energy efficiency compensation model. However, the PUCO determined that certain non-residential customers may opt out of Duke Energy Ohio's energy efficiency initiative. Applications for rehearing of this issue were denied by the PUCO and no further appeals of this issue have been taken.

Duke Energy Indiana Energy Efficiency. In October 2007, Duke Energy Indiana filed its petition with the IURC requesting approval of an alternative regulatory plan to increase its energy efficiency efforts in the state. Duke Energy Indiana seeks approval of a plan that will be available to all customer groups and will compensate Duke Energy Indiana for verified reductions in energy usage. Under the plan, customers would pay for energy efficiency programs through an energy efficiency rider that would be included in their power bill and adjusted annually through a proceeding before the IURC. The energy efficiency rider proposal is based on the save-a-watt compensation model of avoided cost of generation. A number of parties have intervened in the proceeding. Duke Energy Indiana has reached a settlement with all intervenors except one, the Citizens Action Coalition of Indiana, Inc (CAC), and has filed such settlement agreement with the IURC. An evidentiary hearing with the IURC was held on February 27, 2009 and March 2, 2009, and an order is expected in the second half of 2009.

Duke Energy Kentucky Energy Efficiency. On November 15, 2007, Duke Energy Kentucky filed its annual application to continue existing energy efficiency programs, consisting of nine residential and two commercial and industrial programs, and to true-up its gas and electric tracking mechanism for recovery of lost revenues, program costs and shared savings. On February 11, 2008, Duke Energy Kentucky filed a motion to amend its energy efficiency programs and applied to reinstitute a low income Home Energy Assistance Program. The KPSC bifurcated the proposed Home Energy Assistance Program from the other energy efficiency programs. On May 14, 2008, the KPSC approved the energy efficiency programs. On September 25, 2008, the KPSC approved Duke Energy Kentucky's Home Energy Assistance program, making it available for customers at or below 150% of the federal poverty level. On December 1, 2008, Duke Energy Kentucky filed an application for a save-a-watt Energy Efficiency Plan. The application seeks a new energy efficiency recovery mechanism similar to what was proposed in Ohio. On August 21, 2009, the evidentiary hearing with the KPSC scheduled to occur on August 27, 2009 was continued by Order of the KPSC. The Order allows for a brief continuance to allow for additional discovery. A new hearing date will be determined.

Duke Energy Indiana Storm Cost Deferrals. On July 22, 2009, Duke Energy Indiana filed a request with the IURC to defer storm costs associated with a January 27, 2009 ice storm, which caused approximately \$14 million of damage primarily to its distribution system. Duke Energy Indiana has requested to defer the retail jurisdictional portion of the incremental storm costs, which would otherwise be charged as operating expense, until Duke Energy Indiana's next general retail electric rate proceeding. The costs at issue have been charged to operating expense pending an IURC order in this proceeding. Duke Energy Indiana will file its case-in-chief testimony on August 27, 2009 and an evidentiary hearing is scheduled for November 12, 2009.

Capital Expansion Projects.

Edwardsport Integrated Gasification Combined Cycle (IGCC) Plant. On September 7, 2006, Duke Energy Indiana and Southern Indiana Gas and Electric Company d/b/a Vectren Energy Delivery of Indiana (Vectren) filed a joint petition with the IURC seeking a Certificate of Public Convenience and Necessity (CPCN) for the construction of a 630 MW IGCC power plant at Duke Energy Indiana's

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Edwardsport Generating Station in Knox County, Indiana. The facility was initially estimated to cost approximately \$2 billion (including approximately \$120 million of AFUDC). In August 2007, Vectren formally withdrew its participation in the IGCC plant and a hearing was conducted on the CPCN petition based on Duke Energy Indiana owning 100% of the project. On November 20, 2007, the IURC issued an order granting Duke Energy Indiana a CPCN for the proposed IGCC Project, approved the cost estimate of \$1.985 billion and approved the timely recovery of costs related to the project. On January 25, 2008, Duke Energy Indiana received the final air permit from the Indiana Department of Environmental Management. The CAC, Sierra Club, Save the Valley, Inc., and Valley Watch, Inc. have appealed the air permit.

On May 1, 2008, Duke Energy Indiana filed its first semi-annual IGCC Rider and ongoing review proceeding with the IURC as required under the CPCN Order issued by the IURC in November 2007, which approved the IGCC Project. In its filing, Duke Energy Indiana requested approval of a new cost estimate for the IGCC Project of \$2.35 billion (including approximately \$125 million of AFUDC) and for approval of plans to study carbon capture as required by the IURC's November 2007 CPCN Order. An evidentiary hearing was conducted on August 25, 2008. On January 7, 2009, the IURC approved Duke Energy Indiana's request, including the new cost estimate of \$2.35 billion, and cost recovery associated with a study on carbon capture. Duke Energy Indiana was also required to file its plans for studying carbon storage related to the project within 60 days of the order. The OUCC filed a motion of clarification of this order concerning a ratemaking issue related to deferred taxes. The order was not otherwise appealed. The IURC denied the OUCC's motion on April 1, 2009. On November 3, 2008, Duke Energy Indiana filed its second semi-annual IGCC Rider and ongoing review proceeding with the IURC and an evidentiary hearing with the IURC was held on March 9, 2009. On May 13, 2009, the IURC approved Duke Energy Indiana's request in full. On May 1, 2009, Duke Energy Indiana filed its third semi-annual IGCC Rider and ongoing review proceeding with the IURC and an evidentiary hearing is scheduled for August 26, 2009.

Duke Energy Indiana filed a petition with the IURC requesting approval of its plans for studying carbon storage, sequestration and/or enhanced oil recovery (EOR) for the carbon dioxide (CO₂) from the Edwardsport IGCC facility on March 6, 2009. On July 7, 2009, Duke Energy Indiana filed its case-in-chief testimony requesting approval for cost recovery of a \$121 million site assessment and characterization plan for CO₂ sequestration options including deep saline sequestration, depleted oil and gas sequestration and enhanced oil recovery for the CO₂ from the Edwardsport IGCC facility. An evidentiary hearing is scheduled to begin October 13, 2009.

Under the Edwardsport IGCC CPCN order and statutory provisions, Duke Energy Indiana is entitled to recover the costs reasonably incurred in reliance on the CPCN Order. Duke Energy Indiana has begun construction on the Edwardsport IGCC plant and entered into a \$200 million engineering, procurement and construction management agreement with Bechtel Power Corporation in December 2008 in connection with the construction of the plant.

Federal Advanced Clean Coal Tax Credits. Duke Energy Indiana has been awarded approximately \$134 million of federal advanced clean coal tax credits associated with its construction of the Edwardsport IGCC plant. In March 2008, two environmental groups, Appalachian Voices and the Canary Coalition, filed suit against the Federal government challenging the tax credits awarded to incentivize certain clean coal projects. Although Duke Energy Indiana was not a party to the case, the allegations center on the tax incentives provided for Duke Energy Indiana's Edwardsport IGCC plant. The initial complaint alleged a failure to comply with the National Environmental Policy Act. The first amended complaint, filed in August, 2008, added an Endangered Species Act claim and also sought declaratory and injunctive relief against the U.S. Department of Energy and the U.S. Department of the Treasury. On November 10, 2008, the District Court dismissed the case, finding that plaintiffs lacked standing to pursue their claims. The plaintiff's motion for reconsideration of the ruling remains pending.

Other Matters.

Ohio Riser Leak Investigation. In April 2005, the PUCO issued an order opening a statewide investigation into riser leaks in gas pipeline systems throughout Ohio. The investigation followed four explosions since 2000 caused by gas riser leaks, including an April 2000 explosion in Duke Energy Ohio's service area. In November 2006, the PUCO Staff released the expert report, which concluded that certain types of risers are prone to leaks under various conditions, including over-tightening during initial installation. The PUCO Staff recommended that natural gas companies continue to monitor the situation and study the cause of any further riser leaks to determine whether further remedial action is warranted. As of January 1, 2009, Duke Energy Ohio had approximately 80,000 of these risers on its distribution system. If the PUCO orders natural gas companies to replace all of these risers, Duke Energy Ohio estimates a replacement cost of approximately \$40 million. As part of the rate case filed in July 2007 (see "Duke Energy Ohio Gas Rate Case" above), Duke Energy Ohio requested approval from the PUCO to accelerate its riser replacement program. The riser replacement program is contained in the settlement approved by the PUCO and is expected to be completed at the end of 2012.

Duke Energy Indiana SmartGrid and Distributed Renewable Generation Demonstration Project. Duke Energy Indiana filed a petition and case-in-chief testimony supporting its request to build an intelligent distribution grid in Indiana. The proposal requests approval of distribution formula rates or, in the alternative, a SmartGrid Rider to recover the return on and of the capital costs of the build-out and the recovery of incremental operating and maintenance expenses and lost revenues. The petition also includes a pilot program for the installation of small solar photovoltaic and wind generation on customer sites, for approximately \$10 million over a three-year period. Duke Energy Indiana filed supplemental testimony in January 2009 to reflect the impacts of new favorable tax treatment on the cost/benefit analysis for SmartGrid. The intervenors filed testimony generally supporting SmartGrid, but claiming that Duke Energy Indiana's plan was too fast and too large, with not enough customer benefits in terms of time differentiated rate options and behind the meter energy management systems. The intervenors also opposed the distribution formula rate and the rider request claiming that costs should be recovered in a rate case, or possibly deferred. Duke Energy Indiana filed rebuttal testimony agreeing to slow its deployment, and agreeing to work with the parties collaboratively to design time differentiated rate and energy management system pilots. On June 4, 2009, Duke Energy Indiana filed with the IURC a settlement agreement with the OUCC, the CAC, Nucor Corporation, and the Duke Energy Indiana Industrial Group which provided for a full deployment of Duke Energy Indiana's SmartGrid initiative at a slower pace, including cost recovery through a tracking mechanism. The settlement also included increased reporting and monitoring requirements, approval of Duke Energy Indiana's renewable distributed generation pilot and the creation of a collaborative group designed to initiate several time differentiated pricing pilots, an electric vehicle pilot and a home area network pilot. Additionally, the settlement agreement provided for tracker recovery of the costs associated with the SmartGrid initiative, subject to cost recovery caps and a termination date for the tracker. The tracker will also include a reduction in costs associated with the adoption of a new depreciation study. An evidentiary hearing was held on June 29, 2009 and an order from the IURC is expected in the third or fourth quarter of 2009.

Duke Energy Ohio SmartGrid. Duke Energy Ohio filed an application on June 30, 2009 to establish rates for recovering its SmartGrid net costs incurred for gas and electric distribution service through the end of 2008. The rider for recovering electric SmartGrid costs was approved by the PUCO in its order approving the ESP, as discussed above. Duke Energy Ohio proposed its gas SmartGrid rider as part of its most recent gas distribution rate case. The PUCO Staff has begun its audit of the filing but no procedural schedule has been established. Approval of the initial rider rate is expected in the fourth quarter of 2009.

Gibson Unit 4 Outage. In a 2008 fuel clause proceeding, the IURC granted a motion by the Industrial Group and Nucor Corporation to establish a subdocket to examine whether imprudence in Duke Energy Indiana's maintenance practices led to a forced outage at Gibson

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Station Unit 4 during January-March 2008. The outage contributed to notably higher fuel and purchased power costs during the outage. A hearing on this subdocket proceeding was held in January 2009. The IURC authorized Duke Energy Indiana to collect through rates the costs for which it sought recovery in the subdocket proceeding subject to refund (similar to prior subdockets) pending the outcome of this new subdocket related to maintenance practices for Gibson Station Unit 4. An order is expected from the IURC in the third quarter of 2009.

Midwest Independent Transmission System Operator, Inc. (Midwest ISO) Resource Adequacy Filing. On December 28, 2007, the Midwest ISO filed its Electric Tariff Filing Regarding Resource Adequacy in compliance with the FERC's request of Midwest ISO to file Phase II of its long-term Resource Adequacy plan by December 2007. The proposal includes establishment of a resource adequacy requirement in the form of planning reserve margin. On March 26, 2008, the FERC ruled on the Midwest ISO's Resource Adequacy filing and ordered that the new Module E tariff be effective March 27, 2008. This action established a Midwest ISO-wide resource adequacy requirement for the first Planning Year, which began June 2009. In the Order, the FERC, among other things, clarified that States have the authority to set their own Planning Reserve Margins, as long as they are not inconsistent with any reliability standard approved by the FERC.

Midwest ISO's Establishment of an Ancillary Services Market (ASM). On February 25, 2008, the FERC conditionally accepted the Midwest ISO proposal to implement a day-ahead and real-time ASM, including a scarcity pricing proposal. By approving the ASM proposal, the FERC essentially approved the transfer and consolidation of balancing authority for the entire Midwest ISO area. This will allow the Midwest ISO to determine operating reserve requirements and procure operating reserves from all qualified resources from an organized market, in place of the current system of local management and procurement of reserves by the 24 balancing authorities in the Midwest ISO area. The Midwest ISO launched the ASM on January 6, 2009. In January 2008, Duke Energy Indiana and three other Indiana utilities filed a joint petition with the IURC, requesting, among other things, authority to transfer additional balancing authority functions to the Midwest ISO and for recovery of costs incurred under the ASM. On August 13, 2008 the IURC issued an order authorizing the Joint Petitioners to transfer additional balancing authority functions to the Midwest ISO, to participate in the ASM and to defer ASM costs pending a final order in the case. On September 29, 2008, Duke Energy Indiana, Vectren and the OUCC filed a Joint Stipulation and Agreement with the IURC reflecting the settlement by the OUCC with each of these utilities on the cost recovery aspects of the proceeding. In December 2008, Duke Energy Indiana, Vectren, the OUCC, the industrial group and Nucor Corporation met to discuss the cost recovery aspects of the proceeding. On January 6, 2009, a modified Stipulation and Agreement and Modified Settlement terms were filed along with supporting testimony. A hearing was held on February 9, 2009. On June 30, 2009, the IURC issued an order in this proceeding approving the requested cost recovery for the Indiana Midwest ISO utilities, including Duke Energy Indiana. The IURC did not approve the settlement agreement whereby Duke Energy Indiana and Vectren would have been able to retain a share of net excess ASM revenues (where revenues from the sale of ancillary services exceed the costs of purchasing ancillary services on a quarterly basis), noting that it was difficult to determine what ASM-related costs may already be included in the two utilities' base rates, and that the IURC had a preference to treat all Midwest ISO utilities in a consistent manner (two of the utilities did not have such a settlement agreement). As such, the IURC found that it was in the public interest for customers to get full credit of net ASM revenues for all Midwest ISO utilities. The rejection of the settlement agreement is not material to Duke Energy Indiana, as Duke Energy Indiana is still permitted to recover all its ASM-related costs.

FERC 203 Application. On April 23, 2008 (supplemented on May 6, 2008), Duke Energy Ohio and certain affiliates filed an application with the FERC requesting approval to transfer Duke Energy Ohio's electric generating facilities, some of which are designated to serve Ohio customers, to affiliate companies. The FERC filing, if approved, does not obligate Duke Energy Ohio to make the transfer of the electric generating facilities, and does not impact Duke Energy Ohio's current rates. As part of the settlement that was approved by the PUCO on December 17, 2008 (see discussion above), Duke Energy Ohio agreed to withdraw that portion of its application for approval related to the transfer of its generating facilities designated to serve Ohio customers and the PUCO approved of the transfer for the remaining generating facilities. Duke Energy Ohio filed a new application requesting FERC approval to transfer to affiliate companies only the remaining generating facilities not designated to serve Ohio customers, which was conditionally approved by the FERC on February 19, 2009.

Pioneer Transmission LLC Joint Venture. On August 8, 2008, Cinergy announced the formation of a 50-50 joint venture, called Pioneer Transmission LLC (Pioneer Transmission), with American Electric Power Company, Inc. (AEP) to build and operate 240 miles of extra-high-voltage 765KV transmission lines and related facilities in Indiana. Pioneer Transmission will be regulated by the FERC and the IURC. Both Cinergy and AEP own an equal interest in the joint venture and will share equally in the project costs, which are currently estimated at approximately \$1 billion, of which approximately \$500 million is anticipated to be financed by Pioneer Transmission and the remaining amount split equally between Cinergy and AEP. The joint venture will operate in Indiana as a transmission utility. The earliest possible in-service date for the project is in 2014 or 2015. On March 27, 2009, the FERC issued an order granting favorable rate treatment for the project, including requested rate incentives. As is customary in formula rate cases, the FERC set the formula rate that transmission customers would pay for hearing and settlement procedures to address various challenges by intervenors to the inputs and calculations underlying the formula rate. On August 13, 2009, Pioneer Transmission filed an offer of settlement with the FERC, which is intended to resolve the outstanding formula rate issues.

11. Commitments and Contingencies

Environmental

Cinergy is subject to federal, state and local regulations regarding air and water quality, hazardous and solid waste disposal and other environmental matters. These regulations can be changed from time to time, imposing new obligations on Cinergy.

Remediation Activities. Cinergy and its affiliates are responsible for environmental remediation at various contaminated sites. These include some properties that are part of ongoing Cinergy operations, sites formerly owned or used by Cinergy entities, and sites owned by third parties. Remediation typically involves management of contaminated soils and may involve groundwater remediation. Managed in conjunction with relevant federal, state and local agencies, activities vary with site conditions and locations, remedial requirements, complexity and sharing of responsibility. If remediation activities involve statutory joint and several liability provisions, strict liability, or cost recovery or contribution actions, Cinergy or its affiliates could potentially be held responsible for contamination caused by other parties. In some instances, Cinergy may share liability associated with contamination with other potentially responsible parties, and may also benefit from insurance policies or contractual indemnities that cover some or all cleanup costs. All of these sites generally are managed in the normal course of business or affiliate operations. During 2009, Cinergy has recorded additional reserves associated with remediation activities at certain sites and it is anticipated that additional costs associated with remediation activities at certain of its sites will be incurred.

Included in Other within Deferred Credits and Other Liabilities on the Consolidated Balance Sheets were total accruals related to extended environmental-related activities of approximately \$36 million and \$27 million as of June 30, 2009 and December 31, 2008, respectively. These accruals represent Cinergy's provisions for costs associated with remediation activities at some of its current and former sites, as well as other relevant environmental contingent liabilities. Management, in the normal course of business, continually assesses the nature and extent of known or potential environmental-related contingencies and records liabilities when losses become probable and are reasonably estimable. On August 10, 2009, Duke Energy Ohio filed an application with the PUCO for approval to defer costs related to Manufactured Gas Plant site remediation.

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Clean Water Act 316(b). The U.S. Environmental Protection Agency (EPA) finalized its cooling water intake structures rule in July 2004. The rule established aquatic protection requirements for existing facilities that withdraw 50 million gallons or more of water per day from rivers, streams, lakes, reservoirs, estuaries, oceans or other U.S. waters for cooling purposes. Six of the 12 coal-fired generating facilities in which Cinergy is either a whole or partial owner are affected sources under that rule. On April 1, 2009, the U.S. Supreme Court ruled in favor of the appellants that the EPA may consider costs when determining which technology option each site should implement. Depending on how the cost-benefit analysis is incorporated into the revised EPA rule, the analysis could narrow the range of technology options required for each of the 14 affected facilities. Because of the wide range of potential outcomes, Cinergy is unable to estimate its costs to comply at this time.

Clean Air Interstate Rule (CAIR). The EPA finalized its CAIR in May 2005. The CAIR limits total annual and summertime NO_x emissions and annual SO₂ emissions from electric generating facilities across the Eastern U.S. through a two-phased cap-and-trade program. Phase 1 begins in 2009 for NO_x and in 2010 for SO₂. Phase 2 begins in 2015 for both NO_x and SO₂. On March 25, 2008, the U.S. Court of Appeals for the District of Columbia (D.C. Circuit) heard oral argument in a case involving multiple challenges to the CAIR. On July 11, 2008, the D.C. Circuit issued its decision in *North Carolina v. EPA* No. 05-1244 vacating the CAIR. The EPA filed a petition for rehearing on September 24, 2008 with the D.C. Circuit asking the court to reconsider various parts of its ruling vacating the CAIR. In December 2008, the D.C. Circuit issued a decision remanding the CAIR to the EPA without vacatur. The EPA must now conduct a new rulemaking to modify the CAIR in accordance with the court's July 11, 2008 opinion. This decision means that the CAIR as initially finalized in 2005 remains in effect until the new EPA rule takes effect. The court did not impose a deadline or schedule on the EPA. It is uncertain how long the current CAIR will remain in effect or how the new rulemaking will alter the CAIR.

Cinergy plans to spend approximately \$120 million between 2009 and 2013 (approximately \$85 million in Ohio and \$35 million in Indiana) to comply with Phase 1 of the CAIR. Cinergy is currently unable to estimate the costs to comply with any new rule the EPA will issue in the future as a result of the D.C. District Court's December 2008 decision discussed above. The IURC issued an order in 2006 granting Duke Energy Indiana approximately \$1.07 billion in rate recovery to cover its estimated Phase 1 compliance costs of the CAIR and the Clean Air Mercury Rule in Indiana. Duke Energy Ohio will recover most of the depreciation and financing costs related to environmental compliance projects for 2009-2011 through its ESP.

Coal Combustion Product (CCP) Management. Cinergy currently estimates that it will spend approximately \$223 million over the period 2009-2013 to install synthetic caps and liners at existing and new CCP landfills and to convert some of its CCP handling systems from wet to dry systems.

Comprehensive Environmental Response, Compensation, and Liability Act Matter. In August 2008, Duke Energy Ohio received a notice from the EPA that it has been identified as a potentially responsible party under the Comprehensive Environmental Response, Compensation, and Liability Act at the LWD, Inc., Superfund Site in Calvert City, Kentucky. At this time, Duke Energy Ohio does not have any further information regarding the scope of potential liability associated with this matter.

Litigation

New Source Review (NSR). In 1999-2000, the U.S. Department of Justice, acting on behalf of the EPA and joined by various citizen groups and states, filed a number of complaints and notices of violation against multiple utilities across the country for alleged violations of the NSR provisions of the Clean Air Act (CAA). Generally, the government alleges that projects performed at various coal-fired units were major modifications, as defined in the CAA, and that the utilities violated the CAA when they undertook those projects without obtaining permits and installing the best available emission controls for SO₂, NO_x, and particulate matter. The complaints seek injunctive relief to require installation of pollution control technology on various generating units that allegedly violated the CAA, and unspecified civil penalties in amounts of up to \$32,500 per day for each violation. A number of Cinergy's plants have been subject to these allegations. Cinergy asserts that there were no CAA violations because the applicable regulations do not require permitting in cases where the projects undertaken are "routine" or otherwise do not result in a net increase in emissions.

In November 1999, the U.S. brought a lawsuit in the U.S. Federal District Court for the Southern District of Indiana against Cinergy, Duke Energy Ohio and Duke Energy Indiana alleging various violations of the CAA for various projects at six Cinergy owned and co-owned generating stations in the Midwest. Three northeast states and two environmental groups have intervened in the case. A jury trial commenced on May 5, 2008 and jury verdict was returned on May 22, 2008. The jury found in favor of Cinergy, Duke Energy Ohio and Duke Energy Indiana on all but three units at Wabash River. Additionally, the plaintiffs had claimed that Duke Energy Ohio violated an Administrative Consent Order entered into in 1998 between the EPA and Cinergy relating to alleged violations of Ohio's State Implementation Plan (SIP) provisions governing particulate matter at Duke Energy Ohio's W.C. Beckjord Station.

On October 21, 2008, plaintiffs filed a motion for a new liability trial claiming that defendants misled the plaintiffs and the jury by, among other things, not disclosing a consulting agreement with a fact witness and by referring to that witness as "retired" during the liability trial when in fact he was working for Duke Energy under the referenced consulting agreement in connection with the trial. On December 18, 2008, the court granted plaintiffs' motion for a new liability trial on claims for which Cinergy was not previously found liable. That new trial commenced on May 11, 2009. On May 19, 2009, the jury announced its verdict finding in favor of Cinergy on 4 of the remaining 6 projects at issue. The 2 projects in which the jury found violations were undertaken at Units 1 and 3 of the Gallagher Station in Indiana. A remedy trial on those two violations has been scheduled to commence on January 25, 2010.

The remedy trial for violations previously established at the Wabash River and W.C. Beckjord Stations was held during the week of February 2, 2009. On May 29, 2009, the Court issued its remedy ruling and ordered the following relief: (1) Wabash River units 2, 3 & 5 to be permanently retired by September 30, 2009; (2) surrender of SO₂ allowances equal the emissions from Wabash 2, 3 & 5 from May 22, 2008 through September 30, 2009; (3) civil penalty in the amount of \$687,500 for Beckjord violations; and (4) installation of a particulate continuous emissions monitoring system (PM CEMS) at the W.C. Beckjord Station Units 1 and 2. The civil penalty has been paid and Cinergy is currently evaluating its options for appeal. On June 12, 2009, Cinergy filed a motion with the District Court for a Judgment as a Matter of Law and Request for a New Trial. On July 24, 2009, that motion was denied, thereby starting the 60-day appeal timeline.

On April 3, 2008, the Sierra Club filed a lawsuit in the U.S. District Court for the Southern District of Indiana against Duke Energy Indiana and certain affiliated companies. Sierra Club alleges NSR and Title V violations of the CAA at the Edwardsport generating station in Knox County, Indiana. Sierra Club claims that Duke Energy Indiana violated the CAA when it undertook various maintenance projects at Edwardsport without obtaining permits and installing the best available emission controls. Sierra Club states that it intends to file suit for additional alleged violations of the CAA and the Indiana State Implementation Plan. On June 30, 2008, defendants filed a motion to dismiss, or alternatively to stay, this litigation on jurisdictional grounds. The District Court denied that motion and the case is now in the discovery phase. Trial has been set to commence in January 2011.

On July 31, 2009, the EPA served a request for information under section 114 of the CAA on Cinergy and Duke Energy Ohio, requesting information pertaining to various maintenance projects and emissions and operations data relevant to the Miami Fort and W.C. Beckjord stations in Ohio. Cinergy is required to respond to the EPA's section 114 request within 45 days of receipt.

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It is not possible to estimate the damages, if any, that Cinergy might incur in connection with these matters. Ultimate resolution of these matters relating to NSR, even in settlement, could have a material adverse effect on Cinergy's consolidated results of operations, cash flows or financial position. However, Cinergy will pursue appropriate regulatory treatment for any costs incurred in connection with such resolution.

Section 126 Petitions. In March 2004, the state of North Carolina filed a petition under Section 126 of the CAA in which it alleges that sources in 13 upwind states, including Ohio and Indiana, significantly contribute to North Carolina's non-attainment with certain ambient air quality standards. In August 2005, the EPA issued a proposed response to the petition. The EPA proposed to deny the ozone portion of the petition based upon a lack of contribution to air quality by the named states. The EPA also proposed to deny the particulate matter portion of the petition based upon the CAIR Federal Implementation Plan (FIP) that would address the air quality concerns from neighboring states. On April 28, 2006, the EPA denied North Carolina's petition based upon the final CAIR FIP described above. North Carolina has filed a legal challenge to the EPA's denial. Briefing in that case is under way. On March 5, 2009 the D.C. Circuit remanded the case to the EPA for reconsideration. The EPA has conceded that the D.C. Circuit's July 18, 2008 decision in the CAIR litigation, *North Carolina v. EPA* No. 05-1244, discussed above, and a subsequent order issued by the D.C. Circuit on December 23, 2008, have eliminated the legal basis for the EPA's denial of North Carolina's Section 126 petition. At this time, Cinergy cannot predict the outcome of this proceeding.

Carbon Dioxide (CO₂) Litigation. In July 2004, the states of Connecticut, New York, California, Iowa, New Jersey, Rhode Island, Vermont, Wisconsin and the City of New York brought a lawsuit in the U.S. District Court for the Southern District of New York against Cinergy, American Electric Power Company, Inc., American Electric Power Service Corporation, The Southern Company, Tennessee Valley Authority, and Xcel Energy Inc. A similar lawsuit was filed in the U.S. District Court for the Southern District of New York against the same companies by Open Space Institute, Inc., Open Space Conservancy, Inc., and The Audubon Society of New Hampshire. These lawsuits allege that the defendants' emissions of CO₂ from the combustion of fossil fuels at electric generating facilities contribute to global warming and amount to a public nuisance. The complaints also allege that the defendants could generate the same amount of electricity while emitting significantly less CO₂. The plaintiffs are seeking an injunction requiring each defendant to cap its CO₂ emissions and then reduce them by a specified percentage each year for at least a decade. In September 2005, the District Court granted the defendants' motion to dismiss the lawsuit. The plaintiffs have appealed this ruling to the Second Circuit Court of Appeals. Oral arguments were held before the Second Circuit Court of Appeals on June 7, 2006. It is not possible to predict with certainty whether Cinergy will incur any liability or to estimate the damages, if any, that Cinergy might incur in connection with this matter.

Zimmer Generating Station (Zimmer Station) Lawsuit. In November 2004, a citizen of the Village of Moscow, Ohio, the town adjacent to Duke Energy Ohio's Zimmer Station, brought a purported class action in the U.S. District Court for the Southern District of Ohio seeking monetary damages and injunctive relief against Duke Energy Ohio for alleged violations of the CAA, the Ohio SIP, and Ohio laws against nuisance and common law nuisance. The plaintiffs have filed a number of additional notices of intent to sue and two lawsuits raising claims similar to those in the original claim. One lawsuit was dismissed on procedural grounds, and the remaining two have been consolidated. On December 28, 2006, the District Court certified this case as a class action. In March 2009, a settlement in principle was reached with the class plaintiffs, subject to approval by the court. The settlement, as currently structured, will not have a material adverse effect on Cinergy's consolidated results of operations, cash flows or financial position.

Dunavan Waste Superfund Site. In July and October 2005, Duke Energy Indiana received notices from the EPA that it has been identified as a de minimus potentially responsible party under the Comprehensive Environmental Response, Compensation, and Liability Act at the Dunavan Waste Oil Site in Oakwood, Vermilion County, Illinois. At this time, Duke Energy Indiana does not have any further information regarding the scope of potential liability associated with this matter.

Hurricane Katrina Lawsuit. In April 2006, Cinergy was named in the third amended complaint of a purported class action lawsuit filed in the U.S. District Court for the Southern District of Mississippi. Plaintiffs claim that Cinergy, along with numerous other utilities, oil companies, coal companies and chemical companies, are liable for damages relating to losses suffered by victims of Hurricane Katrina. Plaintiffs claim that defendants' greenhouse gas emissions contributed to the frequency and intensity of storms such as Hurricane Katrina. On August 30, 2007, the court dismissed the case. The plaintiffs have filed their appeal to the Fifth Circuit Court of Appeals and oral argument was heard on August 6, 2008. Due to the late recusal of one of the judges on the Fifth Circuit panel, the court held a new oral argument on November 3, 2008. It is not possible to predict with certainty whether Cinergy will incur any liability or to estimate the damages, if any, that Cinergy might incur in connection with this matter.

Ohio Antitrust Lawsuit. In January 2008, four plaintiffs, including individual, industrial and non-profit customers, filed a lawsuit against Duke Energy Ohio in federal court in the Southern District of Ohio. Plaintiffs allege that Duke Energy Ohio (then The Cincinnati Gas & Electric Company (CG&E)), conspired to provide inequitable and unfair price advantages for certain large business consumers by entering into non-public option agreements with such consumers in exchange for their withdrawal of challenges to Duke Energy Ohio's (then CG&E's) pending RSP, which was implemented in early 2005. Duke Energy Ohio denies the allegations made in the lawsuit. Following Duke Energy Ohio's filing of a motion to dismiss plaintiffs' claims, plaintiffs amended their complaint on May 30, 2008. Plaintiffs now contend that the contracts at issue were an illegal rebate which violate antitrust and Racketeer Influenced and Corrupt Organizations (RICO) statutes. Defendants have again moved to dismiss the claims. On March 31, 2009, the District Court granted Duke Energy Ohio's motion to dismiss. Plaintiffs have filed a motion to alter or set aside the judgment.

Asbestos-related Injuries and Damages Claims. Duke Energy Indiana and Duke Energy Ohio have been named as defendants or co-defendants in lawsuits related to asbestos at their electric generating stations. The impact on Cinergy's consolidated results of operations, cash flows or financial position of these cases to date has not been material. Based on estimates under varying assumptions concerning uncertainties, such as, among others: (i) the number of contractors potentially exposed to asbestos during construction or maintenance of Duke Energy Indiana and Duke Energy Ohio generating plants; (ii) the possible incidence of various illnesses among exposed workers; and (iii) the potential settlement costs without federal or other legislation that addresses asbestos tort actions, Cinergy estimates that the range of reasonably possible exposure in existing and future suits over the foreseeable future is not material. This estimated range of exposure may change as additional settlements occur and claims are made and more case law is established.

Other Litigation and Legal Proceedings. Cinergy and its subsidiaries are involved in other legal, tax and regulatory proceedings arising in the ordinary course of business, some of which involve substantial amounts. Cinergy believes that the final disposition of these proceedings will not have a material adverse effect on its consolidated results of operations, cash flows or financial position.

Cinergy has exposure to certain legal matters that are described herein. As of both June 30, 2009 and December 31, 2008, Cinergy has recorded insignificant reserves for these proceedings and exposures. Cinergy expenses legal costs related to the defense of loss contingencies as incurred.

Other Commitments and Contingencies

DEGS of Narrows, L.L.C. Investigation. In October 2006, Cinergy began an internal investigation into improper data reporting to the EPA regarding air emissions under the NO_x Budget Program at Cinergy's DEGS of Narrows, L.L.C. power plant facility in Narrows, Virginia. The investigation has revealed evidence of falsification of data by an employee relating to the quality assurance testing of its continuous emissions monitoring system to monitor heat input and NO_x emissions. In December 2006, Cinergy voluntarily disclosed the potential

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violations to the EPA and Virginia Department of Environmental Quality (VDEQ), and in January 2007, Cinergy made a full written disclosure of the investigation's findings to the EPA and the VDEQ. In December 2007, the EPA issued a notice of violation. On March 19, 2009, the EPA advised that it will not pursue criminal charges against Cinergy, and negotiations can resume resolving the civil violation of the Clean Air Act identified in the December 2007 notice of violation. Cinergy has taken appropriate disciplinary action, including termination, with respect to the employees involved with the false reporting. It is not possible to predict with certainty whether Cinergy will incur any liability or to estimate the damages, if any, that Cinergy might incur in connection with civil proceedings in this matter.

General. Cinergy enters into various fixed-price, non-cancelable commitments to purchase or sell power (tolling arrangements or power purchase contracts) that may or may not be recognized on the Consolidated Balance Sheets. Some of these arrangements may be recognized at market value on the Consolidated Balance Sheets as undesignated hedge contracts or qualifying hedge positions; see Note 9 for additional information related to derivatives.

12. Guarantees and Indemnifications

Cinergy has various financial and performance guarantees and indemnifications, discussed below, which are issued in the normal course of business. Cinergy enters into these arrangements to facilitate commercial transactions with third parties by enhancing the value of the transaction to the third party.

Cinergy has issued performance guarantees to customers and other third parties that guarantee the payment and performance of other parties, including certain non-wholly-owned consolidated entities, as well as guarantees of debt of certain non-consolidated entities and less than wholly-owned consolidated entities. If such entities were to default on payments or performance, Cinergy would be required under the guarantees to make payments on the obligations of the less than wholly-owned entity. The maximum potential amount of future payments Cinergy could have been required to make under these performance guarantees as of June 30, 2009 was approximately \$140 million. Approximately \$37 million of the performance guarantees expire between 2015 and 2019, with the remaining performance guarantees having no contractual expiration.

Cinergy has entered into various indemnification agreements related to purchase and sale agreements and other types of contractual agreements with vendors and other third parties. These agreements typically cover environmental, tax, litigation and other matters, as well as breaches of representations, warranties and covenants. Typically, claims may be made by third parties for various periods of time, depending on the nature of the claim. Cinergy's potential exposure under these indemnification agreements can range from a specified amount, such as the purchase price, to an unlimited dollar amount, depending on the nature of the claim and the particular transaction. Cinergy is unable to estimate the total potential amount of future payments under these indemnification agreements due to several factors, such as the unlimited exposure under certain guarantees.

At June 30, 2009, the amounts of the fair value recorded for the guarantees and indemnifications mentioned above are insignificant, both individually and in the aggregate.

13. Fair Value of Financial Assets and Liabilities

On January 1, 2008, Cinergy adopted SFAS No. 157 for financial instruments and non-financial derivatives. In February 2008, the FASB issued FSP No. 157-2, "Effective Date of FASB Statement No. 157," which delayed the effective date of SFAS No. 157 until January 1, 2009 for non-financial assets and liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis. Accordingly, effective January 1, 2009, Cinergy adopted SFAS No. 157 for non-financial assets and liabilities. Cinergy did not record any cumulative effect adjustment to retained earnings as a result of the adoption of SFAS No. 157.

SFAS No. 157 defines fair value, establishes a framework for measuring fair value in GAAP in the U.S. and expands disclosure requirements about fair value measurements. Under SFAS No. 157, fair value is considered to be the exchange price in an orderly transaction between market participants to sell an asset or transfer a liability at the measurement date. The fair value definition under SFAS No. 157 focuses on an exit price, which is the price that would be received by Cinergy to sell an asset or paid to transfer a liability versus an entry price, which would be the price paid to acquire an asset or received to assume a liability. Although SFAS No. 157 does not require additional fair value measurements, it applies to other accounting pronouncements that require or permit fair value measurements.

Cinergy determines fair value of financial assets and liabilities based on the following fair value hierarchy, as prescribed by SFAS No. 157, which prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Level 1 inputs—unadjusted quoted prices in active markets for identical assets or liabilities that Cinergy has the ability to access. An active market for the asset or liability is one in which transactions for the asset or liability occur with sufficient frequency and volume to provide ongoing pricing information. Cinergy does not adjust quoted market prices on Level 1 inputs for any blockage factor.

Level 2 inputs—inputs other than quoted market prices included in Level 1 that are observable, either directly or indirectly, for the asset or liability. Level 2 inputs include, but are not limited to, quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs other than quoted market prices that are observable for the asset or liability, such as interest rate curves and yield curves observable at commonly quoted intervals, volatilities, credit risk and default rates.

Level 3 inputs—unobservable inputs for the asset or liability.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities- including an amendment of FASB Statement No. 115" (SFAS No. 159), which permits entities to elect to measure many financial instruments and certain other items at fair value. For Cinergy, SFAS No. 159 was effective as of January 1, 2008 and had no impact on amounts presented for periods prior to the effective date. Cinergy does not currently have any financial assets or financial liabilities for which the provisions of SFAS No. 159 have been elected. However, in the future, Cinergy may elect to measure certain financial instruments at fair value in accordance with this standard.

The following tables provide the fair value measurement amounts for assets and liabilities recorded on Cinergy's Consolidated Balance Sheets at fair value at June 30, 2009 and December 31, 2008. Derivative amounts in the table below exclude cash collateral amounts which are disclosed in Note 9.

Notes to Unaudited Consolidated Financial Statements

Description	Total Fair Value Amounts at June 30, 2009	Level 1	Level 2	Level 3
	(in millions)			
Long-term available-for-sale equity securities ^{(c)(d)}	\$ 37	\$ 37	\$ —	\$ —
Long-term available-for-sale debt securities ^{(c)(d)}	32	—	32	—
Derivative assets ^(a)	109	—	—	109
Total Assets	<u>\$ 178</u>	<u>\$ 37</u>	<u>\$ 32</u>	<u>\$ 109</u>
Derivative liabilities ^(b)	(272)	(148)	(44)	(80)
Net (Liabilities) Assets	<u><u>\$(94)</u></u>	<u><u>\$(111)</u></u>	<u><u>\$(12)</u></u>	<u><u>\$ 29</u></u>

- (a) Included in Other within Current Assets and Other within Investments and Other Assets on the Consolidated Balance Sheets.
(b) Included in Other within Current Liabilities and Other within Deferred Credits and Other Liabilities on the Consolidated Balance Sheets.
(c) Included in Other within Investments and Other Assets on the Consolidated Balance Sheets.
(d) See Note 14 for additional information related to investments by major security type.

Description	Total Fair Value Amounts at December 31, 2008	Level 1	Level 2	Level 3
	(in millions)			
Long-term available-for-sale securities ^{(c)(d)}	\$104	\$35	\$69	\$—
Derivative assets ^(a)	131	9	1	121
Total Assets	<u>\$235</u>	<u>\$44</u>	<u>\$70</u>	<u>\$121</u>
Derivative liabilities ^(b)	(255)	(88)	(46)	(121)
Net (Liabilities) Assets	<u><u>\$(20)</u></u>	<u><u>\$(44)</u></u>	<u><u>\$24</u></u>	<u><u>\$—</u></u>

- (a) Included in Other within Current Assets and Other within Investments and Other Assets on the Consolidated Balance Sheets.
(b) Included in Other within Current Liabilities and Other within Deferred Credits and Other Liabilities on the Consolidated Balance Sheets.
(c) Included in Other within Investments and Other Assets on the Consolidated Balance Sheets.
(d) See Note 14 for additional information related to investments by major security type.

The following table provides a reconciliation of beginning and ending balances of assets measured at fair value on a recurring basis where the determination of fair value includes significant unobservable inputs (Level 3):

	Derivatives (net) (in millions)
Three Months Ended June 30, 2009	
Balance at April 1, 2009	\$ 7
Total pre-tax realized or unrealized gains included in earnings:	
Revenue, non-regulated electric and other	(4)
Fuel used in electric generation and purchased power-non-regulated	2
Net purchases, sales, issuances and settlements	12
Total gains included on balance sheet as regulatory asset or liability or as non-current liability	12
Balance at June 30, 2009	<u><u>\$29</u></u>
Three Months Ended June 30, 2008	
Balance at April 1, 2008	\$(29)
Total pre-tax realized or unrealized gains included in earnings:	
Revenue, non-regulated electric and other	65
Total pre-tax losses included in other comprehensive income	(6)
Net purchases, sales, issuances and settlements	(17)
Total gains included on balance sheet as regulatory asset or liability or as non-current liability	33
Balance at June 30, 2008	<u><u>\$ 46</u></u>

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Six Months Ended June 30, 2009

Balance at January 1, 2009	\$ -
Total pre-tax realized or unrealized gains included in earnings:	
Revenue, non-regulated electric and other	8
Fuel used in electric generation and purchased power-non-regulated	3
Total pre-tax gains included in other comprehensive income	1
Net purchases, sales, issuances and settlements	8
Total gains included on balance sheet as regulatory asset or liability or as non-current liability	9
Balance at June 30, 2009	\$ 29
Pre-tax gains included in the Consolidated Statements of Operations related to Level 3 measurements outstanding at June 30, 2009:	
Revenue, non-regulated electric, and other	\$ 3
Fuel used in electric generation and purchased power-non-regulated	5
Total	\$ 8

Six Months Ended June 30, 2008

Balance at January 1, 2008	\$(38)
Total pre-tax realized or unrealized gains included in earnings:	
Revenue, non-regulated electric and other	77
Total pre-tax losses included in other comprehensive income	(9)
Net purchases, sales, issuances and settlements	(31)
Total gains included on balance sheet as regulatory asset or liability or as non-current liability	47
Balance at June 30, 2008	\$ 46
Pre-tax gains included in the Consolidated Statements of Operations related to Level 3 measurements outstanding at June 30, 2008:	
Revenue, non-regulated electric and other	\$ 63
Total	\$ 63

Valuation methods of the primary fair value measurements disclosed above are as follows:

Investments in equity securities: Investments in equity securities are typically valued at the closing price in the principal active market as of the last business day of the quarter. Principal active markets for equity prices include published exchanges such as NASDAQ and NYSE. Foreign equity prices are translated from their trading currency using the currency exchange rate in effect at the close of the principal active market. Cinergy does not adjust prices to reflect for after-hours market activity. The majority of Cinergy's investments in equity securities are valued using Level 1 measurements.

Investments in debt securities: Most debt investments are valued based on a calculation using interest rate curves and credit spreads applied to the terms of the debt instrument (maturity and coupon interest rate) and consider the counterparty credit rating. Most debt valuations are Level 2 measures. If the market for a particular fixed income security is relatively inactive or illiquid, the measurement is a Level 3 measurement. U.S. Treasury debt is typically a Level 1 measurement.

Commodity derivatives: The pricing for commodity derivatives is primarily a calculated value which incorporates the forward price and is adjusted for liquidity (bid-ask spread), credit or non-performance risk (after reflecting credit enhancements such as collateral) and discounted to present value. The primary difference between a Level 2 and a Level 3 measurement has to do with the level of activity in forward markets for the commodity. If the market is relatively inactive, the measurement is deemed to be a Level 3 measurement. Some commodity derivatives are NYMEX contracts, which Cinergy classifies as Level 1 measurements.

Fair Value Disclosures Required Under FSP No. FAS 107-1 and APB 28-1, "Interim Disclosures About Fair Value of Financial Instruments." The fair value of financial instruments, excluding financial assets and certain financial liabilities included in the scope of SFAS No. 157 disclosed in the tables above, is summarized in the following table. Judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, the estimates determined as of June 30, 2009 and December 31, 2008 are not necessarily indicative of the amounts Cinergy could have realized in current markets.

	As of June 30,		As of December 31,	
	2009		2008	
	Book Value	Approximate Fair Value	Book Value	Approximate Fair Value
	(in millions)			
Long-term debt, including current maturities	\$ 5,921	\$ 5,991	\$ 5,085	\$ 4,913

The fair value of cash and cash equivalents, accounts receivable, restricted funds held in trust, accounts payable and notes payable are not materially different from their carrying amounts because of the short-term nature of these instruments and/or because the stated rates approximate market rates.

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14. Investments in Debt and Equity Securities

Pursuant to an order by the IURC, Cinergy invests in debt and equity securities that are held in a grantor trust for investments related to post-retirement benefits other than pension obligations. Cinergy applies SFAS No. 115, "Accounting For Certain Investments in Debt and Equity Securities" (SFAS No. 115), to its investments in debt and equity securities and classifies its investments as available-for-sale, which are carried at estimated fair value based on quoted market prices on the Consolidated Balance Sheets, with unrealized gains and losses related to rate regulated customers deferred as a regulatory liability or asset.

The investments within Cinergy's grantor trust are managed by independent investment managers with discretion to buy, sell and invest pursuant to the objectives set forth by the trust agreements. Therefore, Cinergy has limited oversight of the day-to-day management of these investments. Since day-to-day investment decisions, including buy and sell decisions, are made by the investment manager, the ability to hold investments in unrealized loss positions is outside the control of Cinergy. Accordingly, all unrealized losses associated with equity securities within the grantor trust are considered other-than-temporary and are recognized immediately when the fair value of individual investments is less than the cost basis of the investment. With respect to investments in debt securities within the grantor trust, Cinergy applies the provisions of FSP No. FAS 115-2 and FAS 124-2, "Recognition and Presentation of Other-Than-Temporary Impairments," (FSP No. FAS 115-2 and FAS 124-2). However, pursuant to regulatory accounting, unrealized losses associated with investments in debt and equity securities within the grantor trust related to rate regulated customers are deferred as a regulatory asset, thus there is no immediate impact on the earnings of Cinergy as a result of any other-than-temporary impairments that would otherwise be required to be recognized in earnings under SFAS No. 115 or FSP No. FAS 115-2 and FAS 124-2.

Investments in debt and equity securities are classified as either short-term investments or long-term investments based on management's intent and ability to sell these securities. Since management does not intend to use these investments in current operations, all investments are classified as Other within Investments and Other Assets.

As of June 30, 2009 and December 31, 2008, Cinergy's long-term investments had a fair market value of approximately \$69 million and \$66 million, respectively.

The estimated fair values of other long-term investments classified as available-for-sale are as follows:

	June 30, 2009			December 31, 2008		
	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses (a)	Estimated Fair Value	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses (a)	Estimated Fair Value
	(in millions)					
Equity Securities	\$ —	\$(11)	\$ 37	\$ —	\$(13)	\$ 35
Municipal Bonds	1	—	31	1	(1)	30
Other	—	—	1	—	—	1
Total long-term investments	\$ 1	\$(11)	\$ 69	\$ 1	\$(14)	\$ 66

- (a) Unrealized holding losses are associated with investments held in the Grantor Trust. As discussed above, per a regulatory order from the IURC, Cinergy defers all unrealized gains and losses related to rate regulated customers associated with investments within this Grantor Trust. Accordingly, there is no immediate earnings impact associated with the change in market value of these investments.

Debt securities held at June 30, 2009 mature as follows: \$1 million in less than one year, \$17 million in one to five years, \$8 million in six to ten years and \$6 million thereafter.

The fair values and gross unrealized losses of available-for-sale debt and equity securities which are in an unrealized loss position for which other-than-temporary impairment losses have not been recorded, summarized by investment type and length of time that the securities have been in a continuous loss position, are presented in the tables below as of June 30, 2009 and December 31, 2008.

	As of June 30, 2009		
	Fair Value	Unrealized Loss Position >12 months	Unrealized Loss Position <12 months
	(in millions)		
Equity securities	\$ 37	\$ (1)	\$(10)

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As of December 31, 2008

	Fair Value	Unrealized Loss Position >12 months	Unrealized Loss Position <12 months
	(in millions)		
Equity securities	\$ 33	\$(2)	\$(12)

15. New Accounting Standards

The following new accounting standards were adopted by Cinergy subsequent to June 30, 2008 and the impact of such adoption, if applicable, has been presented in the accompanying Consolidated Financial Statements:

SFAS No. 141R. In December 2007, the FASB issued SFAS No. 141R, which replaces SFAS No. 141, "Business Combinations." SFAS No. 141R retains the fundamental requirements in SFAS No. 141 that the acquisition method of accounting be used for all business combinations and that an acquirer be identified for each business combination. This statement also establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling (minority) interests in an acquiree, and any goodwill acquired in a business combination or gain recognized from a bargain purchase. For Cinergy, SFAS No. 141R must be applied prospectively to business combinations for which the acquisition date occurs on or after January 1, 2009. The impact to Cinergy of applying SFAS No. 141R for periods subsequent to implementation will be dependent upon the nature of any transactions within the scope of SFAS No. 141R. SFAS No. 141R changes the accounting for income taxes related to prior business combinations, such as Cinergy's merger with Duke Energy. Subsequent to the effective date of SFAS No. 141R, the resolution of any tax contingencies relating to Cinergy that existed as of the date of the merger will be required to be reflected in the Consolidated Statements of Operations instead of being reflected as an adjustment to the purchase price via an adjustment to goodwill.

SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements—an amendment of Accounting Research Bulletin (ARB) No. 51" (SFAS No. 160). In December 2007, the FASB issued SFAS No. 160, which amends ARB No. 51, "Consolidated Financial Statements," to establish accounting and reporting standards for the noncontrolling (minority) interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS No. 160 clarified that a noncontrolling interest in a subsidiary is an ownership interest in a consolidated entity that should be reported as equity in the consolidated financial statements. This statement also changed the way the consolidated income statement is presented by requiring consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest. In addition, SFAS No. 160 established a single method of accounting for changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation. For Cinergy, SFAS No. 160 was effective as of January 1, 2009, and has been applied prospectively, except for certain presentation and disclosure requirements that were applied retrospectively. The adoption of SFAS No. 160 impacted the presentation of noncontrolling interests in Cinergy's Consolidated Financial Statements, as well as the calculation of Cinergy's effective tax rate.

SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities—an amendment to FASB Statement No. 133" (SFAS No. 161). In March 2008, the FASB issued SFAS No. 161, which amends and expands the disclosure requirements for derivative instruments and hedging activities prescribed by SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 161 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. Cinergy adopted SFAS No. 161 as of January 1, 2009. The adoption of SFAS No. 161 did not have any impact on Cinergy's consolidated results of operations, cash flows or financial position. See Note 9 for the disclosures required under SFAS No. 161.

The following new accounting standards have been issued, but have not yet been adopted by Cinergy as of June 30, 2009:

FSP No. FAS 132(R)-1, "Employers' Disclosure about Postretirement Benefit Plan Assets" (FSP FAS 132(R)-1). In December 2008, the FASB issued FSP FAS 132(R)-1, which amends SFAS No. 132(R) to require more detailed disclosures about employers' plan assets, concentrations of risk within plan assets, and valuation techniques used to measure the fair value of plan assets. Additionally, companies will be required to disclose their pension assets in a fashion consistent with SFAS No. 157 (i.e., Level 1, 2, and 3 of the fair value hierarchy) along with a roll-forward of the Level 3 values each year. For Cinergy, FSP FAS 132(R)-1 is effective for Cinergy's Year-End Financial Report for the year ended December 31, 2009. The adoption of FSP FAS 132(R)-1 will not have any impact on Cinergy's results of operations, cash flows or financial position.

SFAS No. 166, "Accounting for Transfers of Financial Assets—an amendment of FASB Statement No. 140" (SFAS No. 166). In June 2009, the FASB issued SFAS No. 166, which revises SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" (SFAS No. 140), to require additional information about transfers of financial assets, including securitization transactions, as well as additional information about an enterprise's continuing exposure to the risks related to transferred financial assets. SFAS No. 166 also eliminates the concept of a qualifying special-purpose entity (QSPE) and requires those entities, which were not subject to consolidation under SFAS No. 140 and FASB Interpretation No. 46R, "Consolidation of Variable Interest Entities" (FIN No. 46R), to now be assessed for consolidation. In addition, this statement clarifies and amends the derecognition criteria for transfers of financial assets (including transfers of portions of financial assets) and requires additional disclosures about a transferor's continuing involvement in transferred financial assets. For Cinergy, SFAS No. 166 is effective prospectively for transfers of financial assets occurring on or after January 1, 2010, and early adoption of this statement is prohibited. As described further in Note 17, since 2002, Duke Energy Ohio, Duke Energy Indiana, and Duke Energy Kentucky have sold, on a revolving basis, nearly all of their accounts receivable and related collections through Cinergy Receivables Company (Cinergy Receivables), a bankruptcy-remote QSPE. The securitization transaction was structured to meet the criteria for sale accounting treatment under SFAS No. 140, and accordingly, Cinergy has not consolidated Cinergy Receivables, and the transfers have been accounted for as sales. Upon adoption of SFAS No. 166, the accounting treatment and/or financial statement presentation of Cinergy's accounts receivable securitization programs could potentially be impacted, as Cinergy Receivables must be assessed for consolidation and any transfers of accounts receivables on or after the effective date of SFAS No. 166 would be subject to that statement's amended derecognition criteria for financial assets. Cinergy is currently evaluating the potential impact of the adoption of SFAS No. 166, and is unable to estimate at this time the impact of SFAS No. 166 on its consolidated results of operations, cash flows or financial position.

SFAS No. 167, "Amendments to FASB Interpretation No. 46R" (SFAS No. 167). In June 2009, the FASB issued SFAS No. 167, which amends FIN No. 46R to eliminate the exemption from consolidation for QSPEs, and clarifies, but does not significantly change, the criteria for determining whether an entity meets the definition of a variable interest entity (VIE). SFAS No. 167 also requires an enterprise to qualitatively

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assess the determination of the primary beneficiary of a VIE based on whether that enterprise has both the power to direct matters that most significantly impact the activities of a VIE and the obligation to absorb losses or the right to receive benefits of a VIE that could potentially be significant to a VIE. In addition, SFAS No. 167 modifies FIN No. 46R to require an ongoing evaluation of a VIE's primary beneficiary and amends the types of events that trigger a reassessment of whether an entity is a VIE. Furthermore, SFAS No. 167 requires enterprises to provide additional disclosures about their involvement with VIEs and any significant changes in their risk exposure due to that involvement. For Cinergy, SFAS No. 167 is effective beginning on January 1, 2010, and is applicable to all entities in which Cinergy is involved with, including entities previously subject to the provisions of FIN No. 46R, as well as any QSPEs that exist as of the effective date. Early adoption of SFAS No. 167 is prohibited. Cinergy is currently evaluating the potential impact of the adoption of SFAS No. 167, and is unable to estimate at this time the impact of SFAS No. 167 on its consolidated results of operations, cash flows or financial position.

SFAS No. 168, "The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles" (SFAS No. 168). In June 2009, the FASB issued SFAS No. 168, which identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP. Rules and interpretive releases of the Securities and Exchange Commission (SEC) under authority of federal securities laws are also sources of authoritative GAAP. On the effective date of SFAS No. 168, which is for financial statements issued for interim and annual periods ending after September 15, 2009, the Codification will supersede all then-existing non-SEC accounting and reporting standards. Once the Codification is in effect, all of its content will carry the same level of authority, thus superseding SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles," and the GAAP hierarchy will include only two levels of GAAP: authoritative and non-authoritative. While the adoption of SFAS No. 168 will not have an impact on the accounting followed in Cinergy's consolidated financial statements, SFAS No. 168 will impact the references to authoritative and non-authoritative accounting literature contained within the Notes.

16. Income Taxes and Other Taxes

The taxable income of Cinergy is reflected in Duke Energy's U.S. federal and state income tax returns. Cinergy has a tax sharing agreement with Duke Energy, where the separate return method is used to allocate tax expenses and benefits to the subsidiaries whose investments or results of operations provide these tax expenses and benefits. The accounting for income taxes essentially represents the income taxes that Cinergy would incur if Cinergy were a separate company filing its own tax return as a C-Corporation.

Changes to Unrecognized Tax Benefits

	Increase/ (Decrease)
	(in millions)
Unrecognized Tax Benefits—January 1, 2009	\$ 31
Unrecognized Tax Benefits Changes	
Gross increases—tax positions in prior periods	5
Gross decreases—tax positions in prior periods	(1)
Settlements	(9)
Total Changes	(5)
Unrecognized Tax Benefits—June 30, 2009	\$ 26

At June 30, 2009 and December 31, 2008, Cinergy had approximately \$5 million and \$6 million, respectively, of unrecognized tax benefits that, if recognized, may affect the effective tax rate. Cinergy does not anticipate a significant increase or decrease in unrecognized tax benefits in the next twelve months.

Cinergy has the following tax years open:

Jurisdiction	Tax Years
Federal	2005 and after
State	Closed through 2001, with the exception of any adjustments related to open federal years

The effective tax rate for the three months ended June 30, 2009 was approximately 36.5% as compared to the effective tax rate of approximately 34.2% for the same period in 2008. The effective tax rate for the six months ended June 30, 2009 was approximately 36.7% as compared to the effective tax rate of approximately 35.0% for the same period in 2008. The increase in the effective tax rate for the three and six months ended June 30, 2009 is due primarily to a true-up of prior year taxes related to adjustments to the manufacturing deduction.

Excise Taxes. Certain excise taxes levied by state or local governments are collected by Cinergy from its customers. These taxes, which are required to be paid regardless of Cinergy's ability to collect from the customer, are accounted for on a gross basis. When Cinergy acts as an agent, and the tax is not required to be remitted if it is not collected from the customer, the taxes are accounted for on a net basis. Cinergy's excise taxes accounted for on a gross basis and recorded as operating revenues in the accompanying Consolidated Statements of Operations were approximately \$34 million and \$82 million for the three and six months ended June 30, 2009, respectively, and approximately \$36 million and \$82 million for the three and six months ended June 30, 2008, respectively.

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17. Variable Interest Entities

Accounts Receivable Securitization

Cinergy Receivables Company. During 2002, Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky entered into an agreement to sell certain of their accounts receivable and related collections through Cinergy Receivables, a bankruptcy remote, QSPE. Cinergy Receivables is a wholly-owned limited liability company of Cinergy and was formed in 2002 through a \$5 million equity contribution by Cinergy to purchase certain accounts receivable of Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky. The purpose of the formation of Cinergy Receivables was to improve liquidity at the lowest possible financing cost. As a result of the securitization, Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky sell, on a revolving basis, nearly all of their retail accounts receivable and related collections. The securitization transaction was structured to meet the criteria for sale treatment under SFAS No. 140 and, accordingly, Cinergy does not consolidate Cinergy Receivables and the transfers of receivables are accounted for as sales. Cinergy accounts for Cinergy Receivables under the equity method of accounting and all of the earnings or losses of Cinergy Receivables are therefore reflected in Cinergy's consolidated earnings. However, as discussed further in Note 15, the accounting treatment and/or the financial statement presentation of Cinergy Receivables could potentially be impacted by the adoption of SFAS No. 166 and SFAS No. 167 on January 1, 2010.

The proceeds obtained from the sales of receivables are largely cash but do include a subordinated note from Cinergy Receivables for a portion of the purchase price (typically approximates 25% of the total proceeds). The note, which amounts to approximately \$286 million and \$292 million at June 30, 2009 and December 31, 2008, respectively, is subordinate to senior loans that Cinergy Receivables obtains from commercial paper conduits controlled by unrelated financial institutions. Cinergy Receivables provides credit enhancement related to senior loans in the form of over-collateralization of the purchased receivables. However, the over-collateralization is calculated monthly and does not extend to the entire pool of receivables held by Cinergy Receivables at any point in time. As such, these senior loans do not have recourse to all assets of Cinergy Receivables. These loans provide the cash portion of the proceeds paid to Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky.

This subordinated note is a retained interest (right to receive a specified portion of cash flows from the sold assets) under SFAS No. 140 and is classified within Receivables in the accompanying Consolidated Balance Sheets at June 30, 2009 and December 31, 2008. In addition, Cinergy's investment in Cinergy Receivables constitutes a purchased beneficial interest (purchased right to receive specified cash flows, in this case residual cash flows), which is subordinate to the retained interests held by Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky.

In 2008, Cinergy Receivables and Duke Energy Ohio, Duke Energy Kentucky and Duke Energy Indiana amended the governing purchase and sale agreement to allow Cinergy Receivables to convey its bankrupt receivables to the applicable originator for consideration equal to the fair market value of such receivables as of the disposition date. The amount of bankrupt receivables sold is limited to 1% of aggregate sales of the originator during the most recently completed 12 month period. Cinergy Receivables and Duke Energy Ohio, Duke Energy Kentucky and Duke Energy Indiana completed a sale under this amendment in 2008.

Per the governing purchase and sale agreement, Cinergy Receivables is required to maintain a minimum net worth of \$3 million. In December 2008, Cinergy Receivables recorded a \$15 million increase in its provision for uncollectible accounts which reduced its net worth below the \$3 million threshold. During the first quarter of 2009, Cinergy infused approximately \$3.5 million of equity into Cinergy Receivables to remedy the net worth deficiency. In June 2009, Cinergy Receivables recorded a \$5 million increase in its provision for uncollectible accounts which reduced its net worth below the \$3 million threshold. During July 2009, Cinergy infused \$7 million of equity into Cinergy Receivables to remedy the net worth deficiency. The greater amount of receivables in arrears is partially attributable to the economic downturn starting in 2008 having a negative impact on customers' ability to pay their utility bills. Cinergy Receivables, Duke Energy Ohio, Duke Energy Kentucky and Duke Energy Indiana will continue to monitor arrearages to determine whether an other-than-temporary impairment has occurred.

Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky retain servicing responsibilities for their role as collection agents on the amounts due on the sold receivables. However, Cinergy Receivables assumes the risk of collection on the purchased receivables without recourse to Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky in the event of a loss. While no direct recourse to Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky exists, these entities risk loss in the event collections are not sufficient to allow for full recovery of their retained interests. No servicing asset or liability is recorded since the servicing fee paid to Duke Energy Ohio approximates a market rate.

The carrying values of the retained interests are determined by allocating the carrying value of the receivables between the assets sold and the interests retained based on relative fair value. The key assumptions used in estimating the fair value for 2009 were an anticipated credit loss ratio of 0.6%, a discount rate of 2.8% and a receivable turnover rate of 11.6%. Because (a) the receivables generally turnover in less than two months, (b) credit losses are reasonably predictable due to the broad customer base and lack of significant concentration, and (c) the purchased beneficial interest is subordinate to all retained interests and thus would absorb losses first, the allocated bases of the subordinated notes are not materially different than their face value. The hypothetical effect on the fair value of the retained interests assuming both a 10% and a 20% unfavorable variation in credit losses or discount rates is not material due to the short turnover of receivables and historically low credit loss history. Interest accrues to Duke Energy Ohio, Duke Energy Indiana and Duke Energy Kentucky on the retained interests using the accretable yield method, which generally approximates the stated rate on the notes since the allocated basis and the face value are nearly equivalent. Cinergy records income from Cinergy Receivables in a similar manner. An impairment charge would be recorded against the carrying value of both the retained interests and purchased beneficial interest in the event it is determined that an other-than-temporary impairment has occurred.

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The following table shows the gross and net receivables sold, retained interests, purchased beneficial interest, sales, and cash flows during the three and six months ended June 30, 2009:

	Three Months Ended June 30,	Six Months Ended June 30,
	2009	2009
	(in millions)	
Receivables sold as of June 30,		\$ 585
Less: Retained interests		286
Net receivables sold as of June 30,		\$ 299
Purchased beneficial interest		\$ (2)
Sales		
Receivables sold	\$1,200	\$2,798
Loss recognized on sale	9	22
Cash flows		
Cash proceeds from receivables sold	\$1,166	\$2,781
Collection fees received	-	1
Return received on retained interests	6	14

Cash flows from the sale of receivables are reflected within Operating Activities on the Consolidated Statements of Cash Flows.

Collection fees received in connection with the servicing of transferred accounts receivable are included in Operation, maintenance and other on the Consolidated Statements of Operations.

The loss recognized on the sale of receivables is calculated monthly by multiplying the receivables sold during the month by the required discount which is derived monthly utilizing a three year weighted average formula that considers charge-off history, late charge history, and turnover history on the sold receivables, as well as a component for the time value of money. The discount rate, or component for the time value of money, is calculated monthly by summing the prior month-end LIBOR rate plus a fixed rate of 2.39%.

18. Comprehensive Income and Total Comprehensive Income

Comprehensive Income. Comprehensive income includes net income and all other non-owner changes in equity. The table below provides the components of other comprehensive income and total comprehensive income for the three months ended June 30, 2009 and 2008. Components of other comprehensive income and total comprehensive income for the six months ended June 30, 2009 and 2008 are presented in the Consolidated Statements of Equity and Comprehensive Income.

Total Comprehensive Income

	Three Months Ended June 30,	
	2009	2008
	(in millions)	
Net Income	\$ 85	\$227
Other comprehensive income (loss)		
Foreign currency translation adjustment	3	—
Unrealized losses on available-for-sale securities ^(a)	—	(4)
Cash flow hedges ^(b)	3	(2)
Pension and OPEB-related Adjustments to AOCI ^(c)	16	1
Other comprehensive income (loss), net of tax	22	(5)
Total Comprehensive Income	\$ 107	\$222

(a) Net of \$4 million tax benefit for the three months ended June 30, 2008.

(b) Net of \$2 million tax expense and \$1 million tax benefit for the three months ended June 30, 2009 and 2008, respectively.

(c) Net of \$7 million tax expense and \$1 million tax expense for the three months ended June 30, 2009 and 2008, respectively.

19. Subsequent Events

For information on subsequent events related to significant risks and uncertainties related to customer switching, regulatory matters, commitments and contingencies and variable interest entities, see Notes 1, 10, 11 and 17, respectively. Management has evaluated these Unaudited Consolidated Financial Statements and Notes for subsequent events up through August 26, 2009.