

Marketplace Introduction

In 2002, we served more than one million customers. Our marketplace is the key link between our business and the communities we serve.

Our impact on society in the marketplace is made up of the impact of what we produce and how we buy and sell. How much value or harm do our core products and services produce? Is our approach to marketing, advertising and procurement fair and honest, as well as effective?

In the US, the market environment for electricity companies varies from state to state, depending on the level of deregulation enacted in each jurisdiction.

The electric power industry remains highly regulated at the retail level in much of the US, including Kentucky, although in some parts of the country, including Virginia, it is becoming more competitive as a result of price and supply deregulation and other regulatory changes.

Our primary electric service territories are located in Kentucky, which accounted for 60% of our total revenues in 2002. There is also a small customer base in Virginia and Tennessee.

In contrast to the relatively stable market environment in which our utility businesses operate, our non-utility businesses are largely exposed to changes in wholesale prices for electricity, which have decreased significantly in recent periods, as well as being exposed to increases in fuel costs.

Seasonal variations in US demand for electricity reflect the summer cooling period as the time of peak load requirements, with a lesser peak during the winter heating period, the latter primarily in regions which do not have extensive gas distribution networks. The peak period of retail gas demand is the winter heating period.

We are one of a large number of transmission-owning members of the Midwest Independent Systems Operations (MISO), one of the major regional grid operators in the US. MISO commenced commercial operations on 1 February 2002.

Marketplace

The issues

The Marketplace issues for LG&E Energy, upon which we report here are:

- Utility business;
- Energy trading;
- Non-utility businesses;
- Energy delivery.

Shown below, are these issues mapped against our stakeholder groups to show which issues, we believe, are of most relevance to each stakeholder group.

Stakeholder groups				
E.ON	●	◆	▲	■
E.ON investors	●	◆	▲	■
Govt. & energy regulators	●	◆	▲	■
Environmental regulators	●	—	▲	■
Employees	●	◆	▲	■
Customers	●	◆	▲	■
Communities	●	—	▲	■
External bodies	●	—	▲	■
The media	●	◆	▲	■
Joint venture partners	●	◆	▲	■
Trade unions	●	—	▲	■
Contractors	●	—	▲	■
Suppliers	—	—	—	—
Key ● Utility business ◆ Energy trading ▲ Non-utility business ■ Energy delivery				

Marketplace

Utility business

Our power generation and retail electricity and gas services are divided between two subsidiaries, Louisville Gas & Electric Company (LG&E) and Kentucky Utilities Company (KU).



Louisville Gas & Electric Company (LG&E)

LG&E is a regulated public utility that generates and distributes electricity to approximately 382,000 customers and supplies natural gas to approximately 310,000 customers in Louisville and surrounding areas of Kentucky. LG&E's service area covers approximately 700 square miles in 16 counties. Its coal-fired electric generating plants, which are all equipped with systems to reduce sulphur dioxide (SO₂) emissions, produce nearly all (97%) of LG&E's electricity. The remainder is generated by combustion turbines (2%) and by a hydroelectric power plant (1%). Underground natural gas storage fields assist LG&E in providing economical and reliable gas service to customers. As of 31 December 2002, LG&E owned steam and combustion turbine generating facilities with an attributable capacity of 2,882 MW and a 48 MW hydroelectric facility on the Ohio River.

Total aggregate electricity sales by LG&E in 2002 represented an increase of 6% over 2001. Equivalent gas sales saw an 8% decrease in 2002 against 2001.

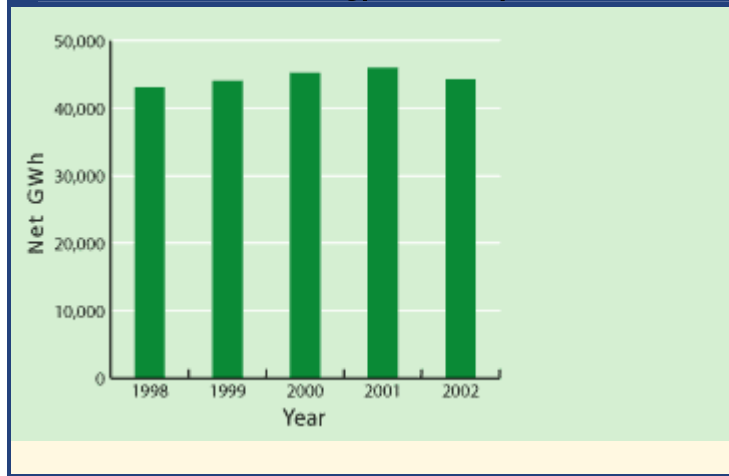


Kentucky Utilities Company (KU)

KU is a regulated public utility engaged in producing, transmitting, distributing and selling electric energy. KU provides electric service to approximately 507,000 customers in 77 counties in central, south-eastern and western Kentucky, including approximately 30,000 customers in south-western Virginia. In Virginia, KU operates under the name Old Dominion Power Company. KU also sells wholesale electric energy to 12 municipalities and fewer than 10 customers in Tennessee. KU's coal-fired electric generating plants produce most (97%) of KU's electricity; the remainder is generated by gas- and oil-fired combustion turbines and a hydroelectric facility. As of 31 December 2002, KU owned steam and combustion turbine generating facilities with an attributable capacity of 4,111 MW and a 24 MW hydroelectric facility.

Total aggregate electricity sales by KU in 2002 represented a 1% increase against 2001.

INDICATOR: LG&E Energy Electricity Generation



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Energy trading

Energy Trading engages in asset-based trading and marketing of energy commodities. It is at the center of the LG&E Energy energy supply structure that serves retail and wholesale electric customers primarily from generation assets that are owned and/or operated by the subsidiaries of LG&E Energy.

Energy Trading serves as the “commercial hub” of the integrated energy business, focusing on optimizing value while assessing and managing the risks associated with the production of electricity and the sale and purchase of interrelated products. This business process ensures that decisions in all business areas are coordinated and made rapidly based on current and future market prices and operating conditions of assets.

The Energy Trading team consists of industry experts in trading and marketing, risk management, and generation asset operations. This team coordinates the delivery of low cost electrical energy to long-term end use customers and the wholesale energy market from generation assets. This team adds further value by orchestrating the short-term sales of excess energy. This process is strictly monitored and controlled to ensure that the levels of exposure are limited and managed within pre-specified guidelines.

Marketplace

Non-utility business

Our non-utility businesses principally comprise the operations of LG&E Capital Corp. (LCC), our primary holding company, and LG&E Marketing Inc. (LEM), our asset-based energy marketing subsidiary. LCC operates ten generating units in western Kentucky through its wholly-owned subsidiary, Western Kentucky Energy Corp. (WKE) and affiliates. It also has ongoing interests in Argentina and stakes in a number of power plants in the US through its wholly-owned subsidiary LG&E Power Inc. We also own CRC-Evans International Inc. (CRC), a company that leases equipment and provides services to the oil and gas pipeline industry.



Western Kentucky Energy (WKE)

Through WKE, LCC has a 25-year lease and operates the generating facilities of Big Rivers Electric Corporation (BREC), a power generation co-operative in western Kentucky, and a coal-fired facility owned by the city of Henderson, Kentucky, aggregating a total generating capacity of 1,771 MW. Over 2002, WKE generated almost 11 TWh of electricity. Approximately 89% of WKE's net generation is used to serve BREC's three member co-operatives and two regional aluminium smelters. Remaining power is sold into the wholesale electric market. As a non-utility entity, WKE is exposed to changes in fuel prices. To mitigate this exposure, WKE has entered into various interim-term fuel supply contracts and is pursuing the use of alternative fuels.

Argentine gas distribution operations

LCC owns interests in Argentine gas distribution operations which provide natural gas to approximately two million customers in Argentina through three distributors: Gas Natural BAN S.A. (Ban), Distribuidora de Gas Del Centro S.A. (Centro) and Distribuidora de Gas Cuyana S.A. (Cuyana). LG&E Energy's operations in Argentina have been affected by the recent economic and political developments in Argentina.



LG&E Power Inc.

LG&E Power Inc., a wholly-owned subsidiary of LCC and its affiliates, owns, operates and maintains interests in six US independent power generation facilities. LCC also owns an interest in a wind power generation facility in Tarifa, Spain, and a minority interest in two US combined cycle gas generation facilities. LG&E Power Services (LPS), an affiliate of LG&E Power, also operates two 63 MW coal-fired facilities in the US under a medium-term operating contract with an independent third party utility.

CRC-Evans

CRC-Evans is a provider of specialised equipment and services used in the construction and rehabilitation of gas and oil transmission pipelines.

LG&E Energy Marketing



LG&E Energy Marketing (LEM) engages in asset-based energy marketing, which primarily involves the marketing of power generated by assets owned or controlled by LG&E Energy and its affiliates.

Marketplace

Energy delivery

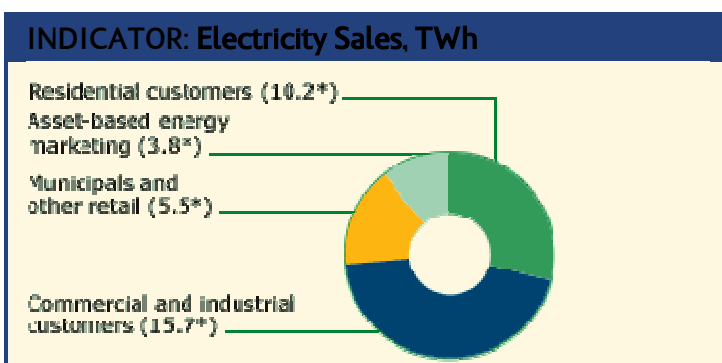
LG&E Energy's Energy Delivery division operates and maintains the electricity and gas distribution networks that serve customers in the states of Kentucky and Virginia. The business is responsible for the distribution assets of the two wholly owned subsidiaries of LG&E – Louisville Gas and Electric and Kentucky Utilities (KU); Virginia customers are served through a separate entity – Old Dominion Power (ODP).

Energy Delivery provides services to customers in over 80 counties in Kentucky and 5 counties in Virginia. Electric and gas distribution service is provided to over 888,000 electricity and almost 310,000 gas customers. The service area served covers about 7,300 square miles, and the distribution system contains more than 19,000 miles of electrical circuit and over 4,100 miles of gas main.

Our aims include:

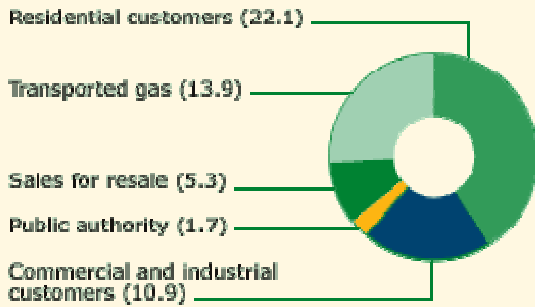
- Delivering electricity to customers that has been generated by LG&E and KU power plants;
- Delivering natural gas supplies to customers from LG&E's underground gas storage system or from interstate pipelines that we contract to transport natural gas from Texas, Louisiana and the Gulf of New Mexico to customers in our area;
- Operating, maintaining, refurbishing and constructing electricity and gas distribution infrastructure;
- Taking prompt and efficient action to ensure safety and restore supply to our customers in the event of customer outages, emergencies, or damage to our network;
- Being committed to the safe, reliable, and low cost supply of energy to our customers;
- Providing prompt and courteous response to customer requests and inquiries including requests for service, billing questions / issues and customer complaints;
- Being socially responsible related to low income customers and their needs for financial assistance and flexible payment options;
- Providing energy conservation options to our customers;
- Striving to achieve award-winning levels of customer satisfaction.

Electricity sales over 2002 are as shown below:



Total electricity sales 35.2TWh

INDICATOR: Gas Sales, billion cubic feet

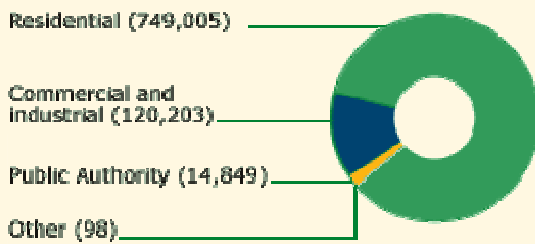


Total gas sales 53.9 billion cubic feet

Customer Numbers

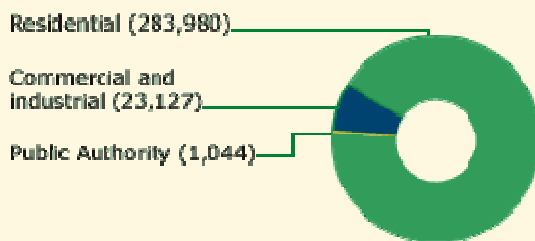
LG&E Energy's average number of customers for 2002 is as shown below.

INDICATOR: Number of Electricity Customers



Total 884,155

INDICATOR: Number of Gas Customers



Total 308,151

Reliability of supply

Energy Delivery is committed to providing reliable and safe electric and gas supply to our customers. Reliability of our system is measured by tracking the system's average length of interruption and the system's average frequency of interruption. Both of these measures exclude major storms in their calculations.

During 2002:

- Customer electricity supply was available 99.99% of the time;
- The average length of electric interruption experienced by our customers (excluding major storms) was 68.9 minutes;
- The average number of electric service interruptions experienced by our customers was 0.82.

Customer satisfaction

LG&E Energy's customer service performance has consistently been rated highly when measured against its competitors. In early 2002, LG&E Energy was rated highest nationally and received its third JD Power and Associates award for Residential Customer Satisfaction. In spring 2002, it was rated highest nationally in customer satisfaction among medium sized businesses.

LG&E Energy measures its overall customer satisfaction on a quarterly basis compared to a panel of similar utilities throughout the Midwest. For 2002, LG&E Energy's satisfaction was ranked highest in three of the four quarters and for the year overall.

A critical component to achieving high customer satisfaction is aggressive management and resolution of customer complaints. It is the Company's policy that all customer complaints be investigated and an initial response provided to the customer within 24 hours. Most complaints are fully resolved within this period. Additionally, all complaints are tracked and the data are shared with managers across the Company.

Assisting the needy

Winter can be a particularly hard time for those in need and LG&E has a number of established ways to provide assistance:

- Community Winterhelp and WinterCare raise over \$1 million each year, which assists low-income customers with their winter heating bills. Contributions are received from customers with LG&E Energy matching a percentage. The funds are administered by third parties with distribution based on income. As well as encouraging customers to donate, LG&E Energy also lets them know how to apply for assistance;
- LG&E is a primary sponsor of Project Warm, an agency that aims to educate low-income customers about conservation and offers assistance to low-income elderly or disabled customers in the LG&E service area. This assistance includes sealing air leaks, adding loft insulation and offering basic energy education. Every year, Project Warm sponsors the Project Warm Blitz – an event where volunteers, including a large number of LG&E employees, work to insulate the homes of eligible individuals and families.

In addition to WinterCare and Project Warm, LG&E Energy offers services and options that assist customers in better managing their energy bills including:

- Credit Counselling;
- Budget Billing;
- Flexible Due Dates;

- **Prepay Metering** – this program also provides information that helps customers reduce their energy usage and as a result, their expenses.



Energy conservation

LG&E Energy maintains a number of commercial and residential energy-saving programs. Together, they are expected to reduce electricity consumption at Louisville Gas and Electric Company and Kentucky Utilities by a total of about 132 MW by 2007. They are also expected to reduce natural gas usage at Louisville Gas and Electric Company by 1.7 million cubic feet by 2007.

- **WeCare** will fund a new home insulation program for low-income customers. The program will provide an audit, energy education and free insulation services to more than 5,400 low-income customers in Kentucky by 2007, significantly reducing their bills;
- **Prepay Metering**, a program providing pre-paid meter users more control over their energy usage. The Company successfully piloted this program and recently received approval from the Kentucky Public Service Commission to offer this option to all customers. Prepay meter equipment provides information about each customer's energy usage patterns and helps them to use energy more efficiently and cost-effectively;
- **Demand Conservation Program** for residential and commercial load management which will reduce peak demand by employing a load control switch on air conditioners and pool pumps;
- **Home energy audits** that educate customers on ways to reduce energy consumption. Low-cost financing is made available for residential energy-related improvements such as installing energy-efficient heating and air-conditioning units;
- **Free energy audits** for commercial customers. Low-cost financing is made available for commercial energy-related improvements such as installing energy-efficient lighting.