Kentucky Power Company

2010 First Quarter Report

Financial Statements

TABLE OF CONTENTS	Page

GLOSSARY OF TERMS

When the following terms and abbreviations appear in the text of this report, they have the meanings indicated below.

Term	Meaning
AEGCo	AEP Generating Company, an AEP electric utility subsidiary.
AEP or Parent	American Electric Power Company, Inc.
AEP East companies	APCo, CSPCo, I&M, KPCo and OPCo.
AEP Power Pool	Members are APCo, CSPCo, I&M, KPCo and OPCo. The Pool shares the generation, cost of generation and resultant wholesale off-system sales of the member companies.
AEP System or the System	American Electric Power System, an integrated electric utility system, owned and operated by AEP's electric utility subsidiaries.
AEPSC	American Electric Power Service Corporation, a service subsidiary providing management and professional services to AEP and its subsidiaries.
AOCI	Accumulated Other Comprehensive Income.
APCo	Appalachian Power Company, an AEP electric utility subsidiary.
CAA	Clean Air Act.
CO_2	Carbon Dioxide and other greenhouse gases.
CSPCo	Columbus Southern Power Company, an AEP electric utility subsidiary.
DETM	Duke Energy Trading and Marketing L.L.C., a risk management counterparty.
Federal EPA	United States Environmental Protection Agency.
FERC	Federal Energy Regulatory Commission.
FTR	Financial Transmission Right, a financial instrument that entitles the holder to receive compensation for certain congestion-related transmission charges that arise when the power grid is congested resulting in differences in locational prices.
GAAP	Accounting Principles Generally Accepted in the United States of America.
I&M	Indiana Michigan Power Company, an AEP electric utility subsidiary.
KGPCo	Kingsport Power Company, an AEP electric distribution subsidiary.
KPCo	Kentucky Power Company, an AEP electric utility subsidiary.
KPSC	Kentucky Public Service Commission.
kV	Kilovolt.
MISO	Midwest Independent Transmission System Operator.
MMBtus	Million British Thermal Units.
MLR	Member load ratio, the method used to allocate AEP Power Pool transactions to its members.
MTM	Mark-to-Market.
MW	Megawatt.
OPCo	Ohio Power Company, an AEP electric utility subsidiary.
OPEB	Other Postretirement Benefit Plans.
OTC	Over the counter.
OVEC	Ohio Valley Electric Corporation, which is 43.47% owned by AEP.
PJM	Pennsylvania – New Jersey – Maryland regional transmission organization.
PSO	Public Service Company of Oklahoma, an AEP electric utility subsidiary.
Risk Management Contracts	Trading and nontrading derivatives, including those derivatives designated as cash flow and fair value hedges.
Rockport Plant	A generating plant, consisting of two 1,300 MW coal-fired generating units near Rockport, Indiana.
RTO	Regional Transmission Organization.

Term	Meaning
S&P	Standard and Poor's.
SIA	System Integration Agreement.
SWEPCo	Southwestern Electric Power Company, an AEP electric utility subsidiary.
Utility Money Pool	AEP System's Utility Money Pool.
VIE	Variable Interest Entity.
WPCo	Wheeling Power Company, an AEP electric distribution subsidiary.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF INCOME
For the Three Months Ended March 31, 2010 and 2009
(in thousands)
(Unaudited)

	2010	2009
REVENUES		
Electric Generation, Transmission and Distribution	$ 162,496	$ 161,249
Sales to AEP Affiliates	11,332	15,423
Other Revenues	90	1,761
TOTAL REVENUES	173,918	178,433
EXPENSES		
Fuel and Other Consumables Used for Electric Generation	52,922	53,041
Purchased Electricity for Resale	4,870	8,617
Purchased Electricity from AEP Affiliates	51,997	48,186
Other Operation	15,085	12,038
Maintenance	8,215	21,345
Depreciation and Amortization	13,095	12,807
Taxes Other Than Income Taxes	3,054	2,346
TOTAL EXPENSES	149,238	158,380
OPERATING INCOME	24,680	20,053
Other Income (Expense):		
Interest Income	45	50
Allowance for Equity Funds Used During Construction	217	(22)
Interest Expense	(9,139)	(7,310)
INCOME BEFORE INCOME TAX EXPENSE	15,803	12,771
Income Tax Expense	6,312	3,317
NET INCOME	$ 9,491	$ 9,454

The common stock of KPCo is wholly-owned by AEP.

See Condensed Notes to Condensed Financial Statements.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF CHANGES IN COMMON SHAREHOLDER'S EQUITY AND COMPREHENSIVE INCOME (LOSS)
For the Three Months Ended March 31, 2010 and 2009
(in thousands)
(Unaudited)

	Common Stock	Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
TOTAL COMMON SHAREHOLDER'S EQUITY – DECEMBER 31, 2008	$ 50,450	$ 208,750	$ 138,749	$ 59	$ 398,008
Common Stock Dividends			(6,750)		(6,750)
SUBTOTAL – COMMON SHAREHOLDER'S EQUITY					391,258
COMPREHENSIVE INCOME					
Other Comprehensive Income, Net of Taxes:					
Cash Flow Hedges, Net of Tax of $134				249	249
NET INCOME			9,454		9,454
TOTAL COMPREHENSIVE INCOME					9,703
TOTAL COMMON SHAREHOLDER'S EQUITY – MARCH 31, 2009	$ 50,450	$ 208,750	$ 141,453	$ 308	$ 400,961
TOTAL COMMON SHAREHOLDER'S EQUITY – DECEMBER 31, 2009	$ 50,450	$ 238,750	$ 143,185	$ (601)	$ 431,784
Common Stock Dividends			(5,000)		(5,000)
SUBTOTAL – COMMON SHAREHOLDER'S EQUITY					426,784
COMPREHENSIVE INCOME					
Other Comprehensive Loss, Net of Taxes:					
Cash Flow Hedges, Net of Tax of $190				(352)	(352)
NET INCOME			9,491		9,491
TOTAL COMPREHENSIVE INCOME					9,139
TOTAL COMMON SHAREHOLDER'S EQUITY – MARCH 31, 2010	$ 50,450	$ 238,750	$ 147,676	$ (953)	$ 435,923

See Condensed Notes to Condensed Financial Statements.

KENTUCKY POWER COMPANY
CONDENSED BALANCE SHEETS
ASSETS
March 31, 2010 and December 31, 2009
(in thousands)
(Unaudited)

	2010	2009
CURRENT ASSETS		
Cash and Cash Equivalents	$ 666	$ 494
Advances to Affiliates	5,817	-
Accounts Receivable:		
Customers	17,999	17,593
Affiliated Companies	8,163	8,692
Accrued Unbilled Revenues	3,465	4,806
Miscellaneous	1,053	1,304
Allowance for Uncollectible Accounts	(857)	(851)
Total Accounts Receivable	29,823	31,544
Fuel	27,274	36,168
Materials and Supplies	17,324	18,248
Risk Management Assets	16,813	13,687
Accrued Tax Benefits	23,959	29,540
Margin Deposits	7,128	5,925
Prepayments and Other Current Assets	2,527	2,416
TOTAL CURRENT ASSETS	131,331	138,022
PROPERTY, PLANT AND EQUIPMENT		
Electric:		
Production	549,537	547,378
Transmission	441,402	438,775
Distribution	576,935	569,389
Other Property, Plant and Equipment	63,741	59,002
Construction Work in Progress	21,984	28,409
Total Property, Plant and Equipment	1,653,599	1,642,953
Accumulated Depreciation and Amortization	519,688	508,806
TOTAL PROPERTY, PLANT AND EQUIPMENT – NET	1,133,911	1,134,147
OTHER NONCURRENT ASSETS		
Regulatory Assets	206,273	206,074
Long-term Risk Management Assets	13,827	9,498
Deferred Charges and Other Noncurrent Assets	38,048	40,178
TOTAL OTHER NONCURRENT ASSETS	258,148	255,750
TOTAL ASSETS	$ 1,523,390	$ 1,527,919

See Condensed Notes to Condensed Financial Statements.

KENTUCKY POWER COMPANY
CONDENSED BALANCE SHEETS
LIABILITIES AND SHAREHOLDER'S EQUITY
March 31, 2010 and December 31, 2009
(Unaudited)

	2010	2009
CURRENT LIABILITIES	(in thousands)	
Advances from Affiliates	$ -	$ 485
Accounts Payable:		
General	33,156	42,595
Affiliated Companies	22,118	27,341
Risk Management Liabilities	7,299	5,190
Customer Deposits	18,883	18,258
Accrued Taxes	12,265	12,625
Accrued Interest	5,789	7,466
Other Current Liabilities	27,424	26,996
TOTAL CURRENT LIABILITIES	126,934	140,956
NONCURRENT LIABILITIES		
Long-term Debt – Nonaffiliated	528,763	528,722
Long-term Debt – Affiliated	20,000	20,000
Long-term Risk Management Liabilities	6,392	4,101
Deferred Income Taxes	307,228	304,549
Regulatory Liabilities and Deferred Investment Tax Credits	35,203	35,678
Employee Benefits and Pension Obligations	49,498	49,843
Deferred Credits and Other Noncurrent Liabilities	13,449	12,286
TOTAL NONCURRENT LIABILITIES	960,533	955,179
TOTAL LIABILITIES	1,087,467	1,096,135
Rate Matters (Note 2)		
Commitments and Contingencies (Note 3)		
COMMON SHAREHOLDER'S EQUITY		
Common Stock – Par Value – $50 Per Share:		
Authorized – 2,000,000 Shares		
Outstanding – 1,009,000 Shares	50,450	50,450
Paid-in Capital	238,750	238,750
Retained Earnings	147,676	143,185
Accumulated Other Comprehensive Income (Loss)	(953)	(601)
TOTAL COMMON SHAREHOLDER'S EQUITY	435,923	431,784
TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	$ 1,523,390	$ 1,527,919

See Condensed Notes to Condensed Financial Statements.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF CASH FLOWS
For the Three Months Ended March 31, 2010 and 2009
(in thousands)
(Unaudited)

	2010	2009
OPERATING ACTIVITIES		
Net Income	$ 9,491	$ 9,454
Adjustments to Reconcile Net Income to Net Cash Flows from Operating Activities:		
Depreciation and Amortization	13,095	12,807
Deferred Income Taxes	950	10,516
Allowance for Equity Funds Used During Construction	(217)	22
Mark-to-Market of Risk Management Contracts	(3,573)	(906)
Fuel Over/Under-Recovery, Net	1,665	13
Change in Other Noncurrent Assets	3,144	2,883
Change in Other Noncurrent Liabilities	(391)	(1,268)
Changes in Certain Components of Working Capital:		
Accounts Receivable, Net	1,721	5,483
Fuel, Materials and Supplies	9,818	2,153
Accounts Payable	(11,191)	(16,213)
Customer Deposits	625	890
Accrued Taxes, Net	5,010	(10,065)
Other Current Assets	(1,242)	(3,342)
Other Current Liabilities	(4,110)	(11,660)
Net Cash Flows from Operating Activities	24,795	767
INVESTING ACTIVITIES		
Construction Expenditures	(12,980)	(19,859)
Change in Advances to Affiliates, Net	(5,817)	-
Acquisitions of Assets	(46)	-
Proceeds from Sales of Assets	142	161
Net Cash Flows Used for Investing Activities	(18,701)	(19,698)
FINANCING ACTIVITIES		
Change in Advances from Affiliates, Net	(485)	25,891
Principal Payments for Capital Lease Obligations	(437)	(180)
Dividends Paid on Common Stock	(5,000)	(6,750)
Net Cash Flows from (Used for) Financing Activities	(5,922)	18,961
Net Increase in Cash and Cash Equivalents	172	30
Cash and Cash Equivalents at Beginning of Period	494	646
Cash and Cash Equivalents at End of Period	$ 666	$ 676
SUPPLEMENTARY INFORMATION		
Cash Paid for Interest, Net of Capitalized Amounts	$ 10,535	$ 17,080
Net Cash Paid for Income Taxes	-	336
Noncash Acquisitions Under Capital Leases	4,108	49
Construction Expenditures Included in Accounts Payable at March 31,	1,980	5,802

See Condensed Notes to Condensed Financial Statements

INDEX TO CONDENSED NOTES TO CONDENSED FINANCIAL STATEMENTS

1. SIGNIFICANT ACCOUNTING MATTERS

General

The unaudited condensed financial statements and footnotes were prepared in accordance with GAAP for interim financial information. Accordingly, they do not include all of the information and footnotes required by GAAP for complete annual financial statements.

In the opinion of management, the unaudited condensed interim financial statements reflect all normal and recurring accruals and adjustments necessary for a fair presentation of the net income, financial position and cash flows for the interim periods. The net income for the three months ended March 31, 2010 is not necessarily indicative of results that may be expected for the year ending December 31, 2010. The condensed financial statements are unaudited and should be read in conjunction with the audited 2009 financial statements and notes thereto, which are included in KPCo's 2009 Annual Report.

Management reviewed subsequent events through April 30, 2010, the date that the 2010 first quarter report was issued.

Variable Interest Entities

The accounting guidance for "Variable Interest Entities" is a consolidation model that considers if a company has a controlling financial interest in a VIE. A controlling financial interest will have both (a) the power to direct the activities of a VIE that most significantly impact the VIE's economic performance and (b) the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. Entities are required to consolidate a VIE when it is determined that they have a controlling financial interest in a VIE and therefore, are the primary beneficiary of that VIE, as defined by the accounting guidance for "Variable Interest Entities." In determining whether KPCo is the primary beneficiary of a VIE, management considers factors such as equity at risk, the amount of the VIE's variability KPCo absorbs, guarantees of indebtedness, voting rights including kick-out rights, the power to direct the VIE and other factors. Management believes that the significant assumptions and judgments were applied consistently. There have been no changes to the reporting of VIEs in the financial statements where it is concluded that KPCo is the primary beneficiary. In addition, KPCo has not provided financial or other support to any VIE that was not previously contractually required.

KPCo holds a significant variable interest in AEPSC and AEGCo. AEPSC provides certain managerial and professional services to KPCo. AEP is the sole equity owner of AEPSC. The costs of the services are based on a direct charge or on a prorated basis and billed to KPCo and other AEP subsidiaries at AEPSC's cost. KPCo and other AEP subsidiaries have not provided financial or other support outside the reimbursement of costs for services rendered. The cost reimbursement nature of AEPSC finances its operations. There are no other terms or arrangements between AEPSC and KPCo and other AEP subsidiaries that could require additional financial support from KPCo and other AEP subsidiaries or expose them to losses outside of the normal course of business. AEPSC and its billings are subject to regulation by the FERC. KPCo and other AEP subsidiaries are exposed to losses to the extent they cannot recover the costs of AEPSC through their normal business operations. KPCo is considered to have a significant interest in the variability of AEPSC due to its activity in AEPSC's cost reimbursement structure. AEPSC is consolidated by AEP. In the event AEPSC would require financing or other support outside the cost reimbursement billings, this financing would be provided by AEP. Total billings from AEPSC for the three months ended March 31, 2010 and 2009 were $9 million and $8 million, respectively. The carrying amount of liabilities associated with AEPSC for the three months ended March 31, 2010 and for the year ended December 31, 2009 were both $4 million. Management estimates the maximum exposure of loss to be equal to the amount of such liability.

AEGCo, a wholly-owned subsidiary of AEP, is consolidated by AEP. AEGCo owns a 50% ownership interest in Rockport Plant Unit 1 and leases a 50% interest in Rockport Plant Unit 2. AEGCo sells all the output from the Rockport Plant to I&M and KPCo. AEP guarantees all the debt obligations of AEGCo. KPCo is considered to have a significant interest in AEGCo due to its transactions. KPCo is exposed to losses to the extent it cannot recover the costs of AEGCo through its normal business operations. Due to AEP management's control over AEGCo, KPCo is not considered the primary beneficiary. In the event AEGCo would require financing or other support outside the billings to KPCo, this financing would be provided by AEP. Total billings from AEGCo for the three months ended March 31, 2010 and 2009 were $24 million and $27 million, respectively. The carrying amount of liabilities associated with AEGCo for the three months ended March 31, 2010 and for the year ended December 31, 2009 were $7 million and $9 million, respectively. Management estimates the maximum exposure of loss to be equal to the amount of such liability.

Related Party Transactions

AEP Power Pool Purchases from OVEC

In January 2010, the AEP Power Pool began purchasing power from OVEC to serve off-system sales and retail sales through June 2010. Purchases serving off-system sales are reported net as a reduction in Electric Generation, Transmission and Distribution revenues and purchases serving retail sales are reported in Purchased Electricity for Resale expenses on KPCo's Condensed Statement of Income. KPCo recorded ($592) thousand in revenue and $444 thousand in expense for the three months ended March 31, 2010.

2. RATE MATTERS

As discussed in KPCo's 2009 Annual Report, KPCo is involved in rate and regulatory proceedings at the FERC and the KPSC. The Rate Matters note within KPCo's 2009 Annual Report should be read in conjunction with this report to gain a complete understanding of material rate matters still pending that could impact net income, cash flows and possibly financial condition. The following discusses ratemaking developments in 2010 and updates KPCo's 2009 Annual Report.

Regulatory Assets Not Yet Being Recovered

Noncurrent Regulatory Assets (excluding fuel)	March 31, 2010	December 31, 2009
	(in thousands)	
Regulatory assets not yet being recovered pending future proceedings to determine the recovery method and timing:		
Regulatory Assets Currently Not Earning a Return		
Storm Related Costs	$ 24,355	$ 24,355
Total Regulatory Assets Not Yet Being Recovered	$ 24,355	$ 24,355

Kentucky Base Rate Filing

In December 2009, KPCo filed a base rate case with the KPSC to increase base revenues by $124 million annually based on an 11.75% return on common equity. The base rate case also requested recovery of $24 million of deferred storm restoration expenses as of March 31, 2010 over a three-year period. In April 2010, the Kentucky Industrial Utility Customers filed testimony with the KPSC which recommends an annual base revenue increase of no more than $41 million based on a 10.1% return on common equity. New rates are expected to become effective in July 2010. If the KPSC denies recovery of the storm restoration regulatory asset, it could reduce future net income and cash flows and impact financial condition.

Validity of Nonstatutory Surcharges

The Franklin County Circuit Court concluded the KPSC did not have the authority to order a surcharge for a gas company subsidiary of Duke Energy absent a full cost of service rate proceeding due to the lack of statutory authority. Both the KPSC and Duke Energy appealed the Franklin County Circuit Court decision. Although this order is not directly applicable, KPCo has existing surcharges which are not specifically authorized by statute. These include KPCo's fuel clause surcharge, the annual Rockport Plant capacity surcharge, the merger surcredit and the off-system sales credit rider. On an annual basis, these surcharges ranged from revenues of approximately $11 million to a reduction of revenues of $5 million due to the volatility of these surcharges. The KPSC asked interested parties to brief the issue in KPCo's fuel cost proceeding. The Kentucky Attorney General responded that the KPCo fuel clause should be invalidated because the KPSC lacked the authority to implement a fuel clause for KPCo without a full rate case review.

The Kentucky Court of Appeals concluded that Duke Energy's surcharge was illegal. However, the order stated that the "decision was premised on the nature of the long-term capital improvements proposed by Duke Energy as distinguished from the fuel and other surcharges that are fluctuating and unanticipated. The latter have been approved by the Kentucky Supreme Court and remain the law." The KPSC filed for a discretionary review of the related Duke Energy case with the Kentucky Supreme Court. Management believes that all of KPCo's variable rate mechanisms are valid and would be upheld if challenged. If KPCo's variable rate mechanisms are found to be invalid, it could reduce future net income and cash flows and impact financial condition.

FERC Rate Matters

Regional Transmission Rate Proceedings at the FERC

Seams Elimination Cost Allocation (SECA) Revenue Subject to Refund

In 2004, AEP eliminated transaction-based through-and-out transmission service (T&O) charges in accordance with FERC orders and collected, at the FERC's direction, load-based charges, referred to as RTO SECA, to partially mitigate the loss of T&O revenues on a temporary basis through March 2006. Intervenors objected to the temporary SECA rates. The FERC set SECA rate issues for hearing and ordered that the SECA rate revenues be collected, subject to refund. The AEP East companies recognized gross SECA revenues of $220 million from 2004 through 2006 when the SECA rates terminated leaving the AEP East companies and ultimately their internal load retail customers to make up the shortfall in revenues. KPCo's portion of recognized gross SECA revenues was $17 million.

In 2006, a FERC Administrative Law Judge (ALJ) issued an initial decision finding that the rate design for the recovery of SECA charges was flawed and that a large portion of the "lost revenues" reflected in the SECA rates should not have been recoverable. The ALJ found that the SECA rates charged were unfair, unjust and discriminatory and that new compliance filings and refunds should be made. The ALJ also found that any unpaid SECA rates must be paid in the recommended reduced amount.

AEP filed briefs jointly with other affected companies noting exceptions to the ALJ's initial decision and asking the FERC to reverse the decision. Management believes that the FERC should reject the ALJ's initial decision because it contradicts prior related FERC decisions, which are presently subject to rehearing. Furthermore, management believes the ALJ's findings on key issues are largely without merit. AEP and SECA ratepayers have been engaged in settlement discussions in an effort to settle the SECA issue. However, if the ALJ's initial decision is upheld in its entirety, it could result in a refund of a portion or all of the unsettled SECA revenues. In December 2009, several parties filed a motion with the U.S. Court of Appeals to force the FERC to resolve the SECA issue.

The AEP East companies provided reserves for net refunds for SECA settlements totaling $44 million applicable to the $220 million of SECA revenues collected. KPCo provided a reserve of $3.3 million.

Settlements approved by the FERC consumed $10 million of the reserve for refunds applicable to $112 million of SECA revenue. The balance in the reserve for future settlements as of March 31, 2010 was $34 million. KPCo's portion of the reserve balance at March 31, 2010 was $2.6 million. As of March 31, 2010, there were no in-process settlements.

Based on the AEP East companies' settlement experience and the expectation that most of the unsettled SECA revenues will be settled, management believes that the reserve is adequate to settle the remaining $108 million of contested SECA revenues. Management cannot predict the ultimate outcome of future settlement discussions or future proceedings at the FERC or court of appeals. However, if the FERC adopts the ALJ's decision and/or AEP cannot settle all of the remaining unsettled claims within the remaining amount reserved for refund, it would reduce future net income and cash flows and impact financial condition.

Modification of the Transmission Agreement (TA)

APCo, CSPCo, I&M, KPCo and OPCo are parties to the TA that provides for a sharing of the cost of transmission lines operated at 138-kV and above and transmission stations containing extra-high voltage facilities. In June 2009, AEPSC, on behalf of the parties to the TA, filed with the FERC a request to modify the TA. Under the proposed amendments, KGPCo and WPCo will be added as parties to the TA. In addition, the amendments would provide for the allocation of PJM transmission costs on the basis of the TA parties' 12-month coincident peak and reimburse transmission revenues based on individual cost of service instead of the MLR method used in the present TA. AEPSC requested the effective date to be the first day of the month following a final non-appealable FERC order. The delayed effective date was approved by the FERC when the FERC accepted the new TA for filing. Settlement discussions are in progress. Once approved by the FERC, management is unable to predict whether the parties to the TA will experience regulatory lag and its effect on future net income and cash flows due to timing of the implementation of the modified TA by various state regulators.

PJM Transmission Formula Rate Filing

AEP filed an application with the FERC in July 2008 to increase its open access transmission tariff (OATT) rates for wholesale transmission service within PJM. The filing sought to implement a formula rate allowing annual adjustments reflecting future changes in the AEP East companies' cost of service. The FERC issued an order conditionally accepting AEP's proposed formula rate and delayed the requested October 2008 effective date for five months. AEP began settlement discussions with the intervenors and the FERC staff which resulted in a settlement that was filed with the FERC in April 2010.

The pending settlement results in a $51 million annual increase beginning in April 2009 for service as of March 2009, of which approximately $7 million is being collected from nonaffiliated customers within PJM. The remaining $44 million is being billed to the AEP East companies and is generally offset by compensation from PJM for use of the AEP East companies' transmission facilities so that net income is not directly affected.

The pending settlement also results in an additional $30 million increase for the first annual update of the formula rate, beginning in August 2009 for service as of July 2009. Approximately $4 million of the increase will be collected from nonaffiliated customers within PJM with the remaining $26 million being billed to the AEP East companies.

Under the formula, an annual update will be filed to be effective July 2010 and each year thereafter. Also, beginning with the July 2010 update, the rates each year will include an adjustment to true-up the prior year's collections to the actual costs for the prior year. Management expects the settlement will be approved by the FERC.

PJM/MISO Market Flow Calculation Errors

During 2009, an analysis conducted by MISO and PJM discovered several instances of unaccounted for power flows on numerous coordinated flowgates. These flows affected the settlement data for congestion revenues and expenses and date back to the start of the MISO market in 2005. PJM has provided MISO an initial analysis of amounts they believe they owe MISO. MISO disputes PJM's methodology.

Settlement discussions between MISO and PJM have been unsuccessful, and as a result, in March 2010, MISO filed two related complaints against PJM at the FERC related to the above claim. MISO seeks to recover a total of approximately $145 million from PJM. Given that PJM passes its costs on to its members, if PJM is held liable for these damages, PJM members, including the AEP East companies, may be held responsible for a share of the refunds or payments PJM is directed to make to MISO. AEP has intervened and filed a protest to one complaint. Management believes that MISO's claims filed at the FERC are without merit and that PJM's right to recover from AEP and other members any damages awarded to MISO is limited. If the FERC orders a settlement above the AEP East companies' reserve related to their estimated portion of PJM additional costs, it could reduce future net income and cash flows and impact financial condition.

Transmission Agreement (TA)

Certain transmission facilities placed in service in 1998 in KPCo's service territory were inadvertently excluded from the AEP East companies' TA calculation. As a result, KPCo did not receive a TA credit for this equipment from the other TA member companies. The amount involved was $7 million annually. It was not discovered until February 2009. KPCo's base electric rates were adjusted only once, in April 2006, during the period in which the error was in effect. Effective January 2009, the allocation was revised to give KPCo its full TA credit prospectively and the KPSC staff and attending intervenor were informed about the revision at a meeting in April 2009. Management does not believe that it is probable that a material retroactive rate adjustment will result.

3. COMMITMENTS, GUARANTEES AND CONTINGENCIES

KPCo is subject to certain claims and legal actions arising in its ordinary course of business. In addition, KPCo's business activities are subject to extensive governmental regulation related to public health and the environment. The ultimate outcome of such pending or potential litigation cannot be predicted. For current proceedings not specifically discussed below, management does not anticipate that the liabilities, if any, arising from such proceedings would have a material adverse effect on the financial statements. The Commitments, Guarantees and Contingencies note within the 2009 Annual Report should be read in conjunction with this report.

GUARANTEES

Liabilities for guarantees are recorded in accordance with the accounting guidance for "Guarantees." There is no collateral held in relation to any guarantees. In the event any guarantee is drawn, there is no recourse to third parties.

Indemnifications and Other Guarantees

Contracts

KPCo enters into certain types of contracts which require indemnifications. Typically these contracts include, but are not limited to, sale agreements, lease agreements, purchase agreements and financing agreements. Generally, these agreements may include, but are not limited to, indemnifications around certain tax, contractual and environmental matters. With respect to sale agreements, exposure generally does not exceed the sale price. Prior to March 31, 2010, KPCo entered into sale agreements including indemnifications with a maximum exposure that was not significant. There are no material liabilities recorded for any indemnifications.

KPCo, along with the other AEP East companies, PSO and SWEPCo, are jointly and severally liable for activity conducted by AEPSC on behalf of the AEP East companies, PSO and SWEPCo related to purchase power and sale activity conducted pursuant to the SIA.

Master Lease Agreements

KPCo leases certain equipment under master lease agreements. GE Capital Commercial Inc. (GE) notified management in November 2008 that they elected to terminate the Master Leasing Agreements in accordance with the termination rights specified within the contract. In 2011, KPCo will be required to purchase all equipment under the lease and pay GE an amount equal to the unamortized value of all equipment then leased. In December 2008 and 2009, management signed new master lease agreements that include lease terms of up to 10 years.

For equipment under the GE master lease agreements that expire in 2011, the lessor is guaranteed receipt of up to 87% of the unamortized balance of the equipment at the end of the lease term. If the fair value of the leased equipment is below the unamortized balance at the end of the lease term, KPCo is committed to pay the difference between the fair value and the unamortized balance, with the total guarantee not to exceed 87% of the unamortized balance. Under the new master lease agreements, the lessor is guaranteed a residual value up to a stated percentage of either the unamortized balance or the equipment cost at the end of the lease term. If the actual fair value of the leased equipment is below the guaranteed residual value at the end of the lease term, KPCo is committed to pay the difference between the actual fair value and the residual value guarantee. At March 31, 2010, the maximum potential loss for these lease agreements was approximately $49 thousand assuming the fair value of the equipment is zero at the end of the lease term. Historically, at the end of the lease term the fair value has been in excess of the unamortized balance.

CONTINGENCIES

Carbon Dioxide Public Nuisance Claims

In 2004, eight states and the City of New York filed an action in Federal District Court for the Southern District of New York against AEP, AEPSC, Cinergy Corp, Xcel Energy, Southern Company and Tennessee Valley Authority. The Natural Resources Defense Council, on behalf of three special interest groups, filed a similar complaint against the same defendants. The actions allege that CO_2 emissions from the defendants' power plants constitute a public nuisance under federal common law due to impacts of global warming and sought injunctive relief in the form of specific emission reduction commitments from the defendants. The trial court dismissed the lawsuits.

In September 2009, the Second Circuit Court of Appeals issued a ruling on appeal remanding the cases to the Federal District Court for the Southern District of New York. The Second Circuit held that the issues of climate change and global warming do not raise political questions and that Congress' refusal to regulate CO_2 emissions does not mean that plaintiffs must wait for an initial policy determination by Congress or the President's administration to secure the relief sought in their complaints. The court stated that Congress could enact comprehensive legislation to regulate CO_2 emissions or that the Federal EPA could regulate CO_2 emissions under existing CAA authorities and that either of these actions could override any decision made by the district court under federal common law. The Second Circuit did not rule on whether the plaintiffs could proceed with their state common law nuisance claims. The defendants' petition for rehearing was denied.

In October 2009, the Fifth Circuit Court of Appeals reversed a decision by the Federal District Court for the District of Mississippi dismissing state common law nuisance claims in a putative class action by Mississippi residents asserting that CO_2 emissions exacerbated the effects of Hurricane Katrina. The Fifth Circuit held that there was no exclusive commitment of the common law issues raised in plaintiffs' complaint to a coordinate branch of government and that no initial policy determination was required to adjudicate these claims. The court granted petitions for rehearing and scheduled oral argument for May 24, 2010. KPCo was initially dismissed from this case without prejudice, but is named as a defendant in a pending fourth amended complaint.

Management believes the actions are without merit and intends to continue to defend against the claims.

Alaskan Villages' Claims

In 2008, the Native Village of Kivalina and the City of Kivalina, Alaska filed a lawsuit in Federal Court in the Northern District of California against AEP, AEPSC and 22 other unrelated defendants including oil and gas companies, a coal company, and other electric generating companies. The complaint alleges that the defendants' emissions of CO_2 contribute to global warming and constitute a public and private nuisance and that the defendants are acting together. The complaint further alleges that some of the defendants, including AEP, conspired to create a false scientific debate about global warming in order to deceive the public and perpetuate the alleged nuisance. The plaintiffs also allege that the effects of global warming will require the relocation of the village at an alleged cost of $95 million to $400 million. In October 2009, the judge dismissed plaintiffs' federal common law claim for nuisance, finding the claim barred by the political question doctrine and by plaintiffs' lack of standing to bring the claim. The judge also dismissed plaintiffs' state law claims without prejudice to refiling in state court. The plaintiffs appealed the decision. Management believes the action is without merit and intends to defend against the claims.

Defective Environmental Equipment

As part of the AEP System's continuing environmental investment program, management chose to retrofit wet flue gas desulfurization systems on one unit of the Big Sandy Plant utilizing the jet bubbling reactor (JBR) technology. Contracts for the project have been temporarily suspended during the early development stage of the project. The retrofits on three units owned by KPCo's affiliates are operational. Due to unexpected operating results, management completed an extensive review of the design and manufacture of the JBR internal components. The review concluded that there are fundamental design deficiencies and that inferior and/or inappropriate materials were selected for the internal fiberglass components. Management initiated discussions with Black & Veatch, the original equipment manufacturer, to develop a repair or replacement corrective action plan. Management intends to pursue contractual and other legal remedies, if management is unable to resolve these issues with Black & Veatch. If KPCo is unsuccessful in obtaining reimbursement for the work required to remedy this situation, the cost of repair or replacement could have an adverse impact on construction costs, net income, cash flows and financial condition.

4. BENEFIT PLANS

KPCo participates in an AEP sponsored qualified pension plan and two unfunded nonqualified pension plans. A substantial majority of employees are covered by the qualified plan or both the qualified and a nonqualified pension plan. In addition, KPCo participates in OPEB plans sponsored by AEP to provide medical and life insurance benefits for retired employees.

Components of Net Periodic Benefit Cost

The following table provides the components of AEP's net periodic benefit cost for the plans for the three months ended March 31, 2010 and 2009:

	Pension Plans		Other Postretirement Benefit Plans	
	Three Months Ended March 31,		Three Months Ended March 31,	
	2010	2009	2010	2009
	(in millions)			
Service Cost	$ 28	$ 26	$ 12	$ 10
Interest Cost	63	63	28	27
Expected Return on Plan Assets	(78)	(80)	(26)	(20)
Amortization of Transition Obligation	-	-	7	7
Amortization of Net Actuarial Loss	22	15	7	11
Net Periodic Benefit Cost	$ 35	$ 24	$ 28	$ 35

The following table provides KPCo's net periodic benefit cost for the plans for the three months ended March 31, 2010 and 2009:

	Pension Plans		Other Postretirement Benefit Plans	
	Three Months Ended March 31,			
	2010	2009	2010	2009
	(in thousands)			
Net Periodic Benefit Costs	$ 749	$ 555	$ 598	$ 808

5. BUSINESS SEGMENTS

KPCo has one reportable segment, an integrated electricity generation, transmission and distribution business. KPCo's other activities are insignificant.

6. DERIVATIVES AND HEDGING

OBJECTIVES FOR UTILIZATION OF DERIVATIVE INSTRUMENTS

KPCo is exposed to certain market risks as a power producer and marketer of wholesale electricity, coal and emission allowances. These risks include commodity price risk, interest rate risk and credit risk. These risks represent the risk of loss that may impact KPCo due to changes in the underlying market prices or rates. AEPSC, on behalf of KPCo, manages these risks using derivative instruments.

STRATEGIES FOR UTILIZATION OF DERIVATIVE INSTRUMENTS TO ACHIEVE OBJECTIVES

The strategy surrounding the use of derivative instruments focuses on managing risk exposures, future cash flows and creating value based on open trading positions by utilizing both economic and formal hedging strategies. To accomplish these objectives, AEPSC, on behalf of KPCo, primarily employs risk management contracts including physical forward purchase and sale contracts, financial forward purchase and sale contracts and financial swap instruments. Not all risk management contracts meet the definition of a derivative under the accounting guidance for "Derivatives and Hedging." Derivative risk management contracts elected normal under the normal purchases and normal sales scope exception are not subject to the requirements of this accounting guidance.

AEPSC, on behalf of KPCo, enters into electricity, coal, natural gas, interest rate and to a lesser degree heating oil, gasoline, emission allowance and other commodity contracts to manage the risk associated with the energy business. AEPSC, on behalf of KPCo, enters into interest rate derivative contracts in order to manage the interest rate exposure associated with KPCo's long-term commodity derivative portfolio. For disclosure purposes, such risks are grouped as "Commodity," as these risks are related to energy risk management activities. From time to time, AEPSC, on behalf of KPCo, also engages in risk management of interest rate risk associated with debt financing. The amount of risk taken is determined by the Commercial Operations and Finance groups in accordance with the established risk management policies as approved by the Finance Committee of AEP's Board of Directors.

The following tables represent the gross notional volume of KPCo's outstanding derivative contracts as of March 31, 2010 and December 31, 2009:

Notional Volume of Derivative Instruments

	Volume		
	March 31, 2010	**December 31, 2009**	**Unit of Measure**
	(in thousands)		
Commodity:			
Power	32,630	38,509	MWHs
Coal	3,909	2,230	Tons
Natural Gas	2,515	3,600	MMBtus
Heating Oil and Gasoline	320	306	Gallons
Interest Rate	$ 2,712	$ 4,239	USD

Fair Value Hedging Strategies

AEPSC, on behalf of KPCo, enters into interest rate derivative transactions as part of an overall strategy to manage the mix of fixed-rate and floating-rate debt. Certain interest rate derivative transactions effectively modify KPCo's exposure to interest rate risk by converting a portion of KPCo's fixed-rate debt to a floating rate. Provided specific criteria are met, these interest rate derivatives are designated as fair value hedges.

Cash Flow Hedging Strategies

AEPSC, on behalf of KPCo, enters into and designates as cash flow hedges certain derivative transactions for the purchase and sale of electricity, coal, heating oil and natural gas ("Commodity") in order to manage the variable price risk related to the forecasted purchase and sale of these commodities. Management monitors the potential impacts of commodity price changes and, where appropriate, enters into derivative transactions to protect profit margins for a portion of future electricity sales and fuel or energy purchases. KPCo does not hedge all commodity price risk.

KPCo's vehicle fleet is exposed to gasoline and diesel fuel price volatility. AEPSC, on behalf of KPCo, enters into financial gasoline and heating oil derivative contracts in order mitigate price risk of future fuel purchases. For disclosure purposes, these contracts are included with other hedging activity as "Commodity." KPCo does not hedge all fuel price risk.

AEPSC, on behalf of KPCo, enters into a variety of interest rate derivative transactions in order to manage interest rate risk exposure. KPCo enters into interest rate derivative contracts to manage interest rate exposure related to anticipated borrowings of fixed-rate debt. The anticipated fixed-rate debt offerings have a high probability of occurrence as the proceeds will be used to fund existing debt maturities and projected capital expenditures. KPCo does not hedge all interest rate exposure.

ACCOUNTING FOR DERIVATIVE INSTRUMENTS AND THE IMPACT ON KPCo's FINANCIAL STATEMENTS

The accounting guidance for "Derivatives and Hedging" requires recognition of all qualifying derivative instruments as either assets or liabilities in the balance sheet at fair value. The fair values of derivative instruments accounted for using MTM accounting or hedge accounting are based on exchange prices and broker quotes. If a quoted market price is not available, the estimate of fair value is based on the best information available including valuation models that estimate future energy prices based on existing market and broker quotes, supply and demand market data and assumptions. In order to determine the relevant fair values of the derivative instruments, KPCo applies valuation adjustments for discounting, liquidity and credit quality.

Credit risk is the risk that a counterparty will fail to perform on the contract or fail to pay amounts due. Liquidity risk represents the risk that imperfections in the market will cause the price to vary from estimated fair value based upon prevailing market supply and demand conditions. Since energy markets are imperfect and volatile, there are inherent risks related to the underlying assumptions in models used to fair value risk management contracts. Unforeseen events may cause reasonable price curves to differ from actual price curves throughout a contract's term and at the time a contract settles. Consequently, there could be significant adverse or favorable effects on future net income and cash flows if market prices are not consistent with management's estimates of current market consensus for forward prices in the current period. This is particularly true for longer term contracts. Cash flows may vary based on market conditions, margin requirements and the timing of settlement of KPCo's risk management contracts.

According to the accounting guidance for "Derivatives and Hedging," KPCo reflects the fair values of derivative instruments subject to netting agreements with the same counterparty net of related cash collateral. For certain risk management contracts, KPCo is required to post or receive cash collateral based on third party contractual agreements and risk profiles. For the March 31, 2010 and December 31, 2009 balance sheets, KPCo netted $2.2 million and $800 thousand, respectively, of cash collateral received from third parties against short-term and long-term risk management assets and $11 million and $6.4 million, respectively, of cash collateral paid to third parties against short-term and long-term risk management liabilities.

The following tables represent the gross fair value impact of KPCo's derivative activity on the Condensed Balance Sheet as of March 31, 2010 and December 31, 2009:

Fair Value of Derivative Instruments
March 31, 2010

	Risk Management Contracts	Hedging Contracts			
Balance Sheet Location	**Commodity (a)**	**Commodity (a)**	**Interest Rate (a)**	**Other (a) (b)**	**Total**
			(in thousands)		
Current Risk Management Assets	$ 104,953	$ 1,036	$ -	$ (89,176)	$ 16,813
Long-term Risk Management Assets	48,143	57	-	(34,373)	13,827
Total Assets	153,096	1,093	-	(123,549)	30,640
Current Risk Management Liabilities	99,551	1,713	-	(93,965)	7,299
Long-term Risk Management Liabilities	45,725	189	-	(39,522)	6,392
Total Liabilities	145,276	1,902	-	(133,487)	13,691
Total MTM Derivative Contract Net Assets (Liabilities)	$ 7,820	$ (809)	$ -	$ 9,938	$ 16,949

Fair Value of Derivative Instruments
December 31, 2009

Balance Sheet Location	Risk Management Contracts Commodity (a)	Hedging Contracts Commodity (a)	Hedging Contracts Interest Rate (a)	Other (a) (b)	Total
			(in thousands)		
Current Risk Management Assets	$ 66,858	$ 748	$ -	$ (53,919)	$ 13,687
Long-term Risk Management Assets	26,571	-	-	(17,073)	9,498
Total Assets	93,429	748	-	(70,992)	23,185
Current Risk Management Liabilities	62,216	1,024	-	(58,050)	5,190
Long-term Risk Management Liabilities	23,879	16	-	(19,794)	4,101
Total Liabilities	86,095	1,040	-	(77,844)	9,291
Total MTM Derivative Contract Net Assets (Liabilities)	$ 7,334	$ (292)	$ -	$ 6,852	$ 13,894

(a) Derivative instruments within these categories are reported gross. These instruments are subject to master netting agreements and are presented in the Condensed Balance Sheets on a net basis in accordance with the accounting guidance for "Derivatives and Hedging."
(b) Amounts represent counterparty netting of risk management and hedging contracts, associated cash collateral in accordance with the accounting guidance for "Derivatives and Hedging" and dedesignated risk management contracts.

The table below presents KPCo's activity of derivative risk management contracts for the three months ended March 31, 2010 and 2009:

Amount of Gain (Loss) Recognized on
Risk Management Contracts
For the Three Months Ended March 31, 2010 and 2009

Location of Gain (Loss)	2010	2009
	(in thousands)	
Electric Generation, Transmission and Distribution Revenues	$ 4,635	$ 8,049
Sales to AEP Affiliates	(742)	(1,526)
Regulatory Assets (a)	-	-
Regulatory Liabilities (a)	539	1,464
Total Gain on Risk Management Contracts	$ 4,432	$ 7,987

(a) Represents realized and unrealized gains and losses subject to regulatory accounting treatment recorded as either current or non-current classifications within the balance sheet.

Certain qualifying derivative instruments have been designated as normal purchase or normal sale contracts, as provided in the accounting guidance for "Derivatives and Hedging." Derivative contracts that have been designated as normal purchases or normal sales under that accounting guidance are not subject to MTM accounting treatment and are recognized in the Condensed Statements of Income on an accrual basis.

KPCo's accounting for the changes in the fair value of a derivative instrument depends on whether it qualifies for and has been designated as part of a hedging relationship and further, on the type of hedging relationship. Depending on the exposure, Management designates a hedging instrument as a fair value hedge or a cash flow hedge.

For contracts that have not been designated as part of a hedging relationship, the accounting for changes in fair value depends on whether the derivative instrument is held for trading purposes. Realized gains and losses on derivative instruments held for trading purposes are included in Revenues on a net basis in KPCo's Condensed Statements of Income. Realized gains and losses on derivative instruments not held for trading purposes are included in Revenues or Expenses on KPCo's Condensed Statements of Income depending on the relevant facts and circumstances. Unrealized and realized gains and losses for both trading and non-trading derivative instruments are recorded as regulatory assets (for losses) or regulatory liabilities (for gains), in accordance with the accounting guidance for "Regulated Operations."

Accounting for Fair Value Hedging Strategies

For fair value hedges (i.e. hedging the exposure to changes in the fair value of an asset, liability or an identified portion thereof attributable to a particular risk), KPCo recognizes the gain or loss on the derivative instrument as well as the offsetting gain or loss on the hedged item associated with the hedged risk in Net Income during the period of change.

KPCo records realized gains or losses on interest rate swaps that qualify for fair value hedge accounting treatment and any offsetting changes in the fair value of the debt being hedged, in Interest Expense on KPCo's Condensed Statements of Income. During the three months ended March 31, 2010 and 2009, KPCo did not employ any fair value hedging strategies.

Accounting for Cash Flow Hedging Strategies

For cash flow hedges (i.e. hedging the exposure to variability in expected future cash flows that is attributable to a particular risk), KPCo initially reports the effective portion of the gain or loss on the derivative instrument as a component of Accumulated Other Comprehensive Income (Loss) on the Condensed Balance Sheets until the period the hedged item affects Net Income. KPCo records hedge ineffectiveness as a regulatory asset (for losses) or a regulatory liability (for gains).

Realized gains and losses on derivatives transactions for the purchase and sale of electricity, coal, heating oil and natural gas designated as cash flow hedges are included in Revenues, Fuel and Other Consumables Used for Electric Generation or Purchased Electricity for Resale in KPCo's Condensed Statements of Income, or in Regulatory Assets or Regulatory Liabilities on KPCo's Condensed Balance Sheet, depending on the specific nature of the risk being hedged. During the three months ended March 31, 2010 and 2009, KPCo designated commodity derivatives as cash flow hedges.

KPCo reclassifies gains and losses on financial fuel derivative contracts designated as cash flow hedges from Accumulated Other Comprehensive Income (Loss) on its Condensed Balance Sheets into Other Operation expense, Maintenance expense or Depreciation and Amortization expense, as it relates to capital projects, on the Condensed Statements of Income. During the three months ended March 31, 2010 and 2009, KPCo designated cash flow hedging strategies for forecasted fuel purchases.

KPCo reclassifies gains and losses on interest rate derivative hedges related to debt financings from Accumulated Other Comprehensive Income (Loss) into Interest Expense in those periods in which hedged interest payments occur. During the three months ended March 31, 2010 and 2009, KPCo did not employ any cash flow hedging strategies for interest rates.

During the three months ended March 31, 2010 and 2009, hedge ineffectiveness was immaterial or nonexistent for all hedge strategies disclosed above.

The following tables provide details on designated, effective cash flow hedges included in AOCI on KPCo's Condensed Balance Sheets and the reasons for changes in cash flow hedges for the three months ended March 31, 2010 and 2009. All amounts in the following table are presented net of related income taxes.

Total Accumulated Other Comprehensive Income (Loss) Activity for Cash Flow Hedges
For the Three Months Ended March 31, 2010

	Commodity	Interest Rate	Total
		(in thousands)	
Balance in AOCI as of January 1, 2010	$ (138)	$ (463)	$ (601)
Changes in Fair Value Recognized in AOCI	(528)	-	(528)
Amount of (Gain) or Loss Reclassified from AOCI to Income Statement/within Balance Sheet:			
Electric Generation, Transmission and Distribution Revenues	25	-	25
Other Operation Expense	(2)	-	(2)
Maintenance Expense	(3)	-	(3)
Purchased Electricity for Resale	143	-	143
Interest Expense	-	15	15
Property, Plant and Equipment	(2)	-	(2)
Balance in AOCI as of March 31, 2010	$ (505)	$ (448)	$ (953)

Total Accumulated Other Comprehensive Income (Loss) Activity for Cash Flow Hedges
For the Three Months Ended March 31, 2009

	Commodity	Interest Rate	Total
		(in thousands)	
Balance in AOCI as of January 1, 2009	$ 584	$ (525)	$ 59
Changes in Fair Value Recognized in AOCI	38	-	38
Amount of (Gain) or Loss Reclassified from AOCI to Income Statement/within Balance Sheet			
Electric Generation, Transmission and Distribution Revenues	(233)	-	(233)
Purchased Electricity for Resale	428	-	428
Interest Expense	-	16	16
Balance in AOCI as of March 31, 2009	$ 817	$ (509)	$ 308

Cash flow hedges included in Accumulated Other Comprehensive Income (Loss) on KPCo's Condensed Balance Sheets at March 31, 2010 and December 31, 2009 were:

Impact of Cash Flow Hedges on the Condensed Balance Sheet
March 31, 2010

	Commodity	Interest Rate	Total
		(in thousands)	
Hedging Assets (a)	$ 155	$ -	$ 155
Hedging Liabilities (a)	(964)	-	(964)
AOCI Loss Net of Tax	(505)	(448)	(953)
Portion Expected to be Reclassified to Net Income During the Next Twelve Months	(419)	(60)	(479)

Impact of Cash Flow Hedges on the Condensed Balance Sheet
December 31, 2009

	Commodity	Interest Rate	Total
		(in thousands)	
Hedging Assets (a)	$ 422	$ -	$ 422
Hedging Liabilities (a)	(714)	-	(714)
AOCI Loss Net of Tax	(138)	(463)	(601)
Portion Expected to be Reclassified to Net Income During the Next Twelve Months	(127)	(60)	(187)

(a) Hedging Assets and Hedging Liabilities are included in Risk Management Assets and Liabilities on KPCo's Condensed Balance Sheets.

The actual amounts that KPCo reclassifies from Accumulated Other Comprehensive Income (Loss) to Net Income can differ from the estimate above due to market price changes. As of March 31, 2010, the maximum length of time that KPCo is hedging (with contracts subject to the accounting guidance for "Derivatives and Hedging") exposure to variability in future cash flows related to forecasted transactions is 21 months.

Credit Risk

AEPSC, on behalf of KPCo, limits credit risk in KPCo's wholesale marketing and trading activities by assessing the creditworthiness of potential counterparties before entering into transactions with them and continuing to evaluate their creditworthiness on an ongoing basis. AEPSC, on behalf of KPCo, uses Moody's, S&P and current market-based qualitative and quantitative data to assess the financial health of counterparties on an ongoing basis. If an external rating is not available, an internal rating is generated utilizing a quantitative tool developed by Moody's to estimate probability of default that corresponds to an implied external agency credit rating.

AEPSC, on behalf of KPCo, uses standardized master agreements which may include collateral requirements. These master agreements facilitate the netting of cash flows associated with a single counterparty. Cash, letters of credit and parental/affiliate guarantees may be obtained as security from counterparties in order to mitigate credit risk. The collateral agreements require a counterparty to post cash or letters of credit in the event an exposure exceeds the established threshold. The threshold represents an unsecured credit limit which may be supported by a parental/affiliate guaranty, as determined in accordance with AEP's credit policy. In addition, collateral agreements allow for termination and liquidation of all positions in the event of a failure or inability to post collateral.

Collateral Triggering Events

Under a limited number of derivative and non-derivative counterparty contracts primarily related to pre-2002 risk management activities and under the tariffs of the RTOs and Independent System Operators (ISOs), KPCo is obligated to post an amount of collateral if certain credit ratings decline below investment grade. The amount of collateral required fluctuates based on market prices and total exposure. On an ongoing basis, AEP's risk management organization assesses the appropriateness of these collateral triggering items in contracts. Management believes that a downgrade below investment grade is unlikely. The following table represents the aggregate fair value of such derivative contracts, the amount of collateral KPCo would have been required to post for all derivative and non-derivative contracts if the credit ratings had declined below investment grade and how much was attributable to RTO and ISO activities as of March 31, 2010 and December 31, 2009:

	Aggregate Fair Value of Derivative Contracts	Amount of Collateral KPCo Would Have Been Required to Post	Amount Attributable to RTO and ISO Activities
		(in thousands)	
March 31, 2010	$ 520	$ 1,540	$ 1,540
December 31, 2009	449	1,700	1,600

In addition, a majority of KPCo's non-exchange traded commodity contracts contain cross-default provisions that, if triggered, would permit the counterparty to declare a default and require settlement of the outstanding payable. These cross-default provisions could be triggered if there was a non-performance event under borrowed debt in excess of $50 million. On an ongoing basis, AEP's risk management organization assesses the appropriateness of these cross-default provisions in the contracts. Management believes that a non-performance event under these provisions is unlikely. The following table represents the fair value of these derivative liabilities subject to cross-default provisions prior to consideration of contractual netting arrangements, the amount this exposure has been reduced by cash collateral posted by KPCo and if a cross-default provision would have been triggered, the settlement amount that would be required after considering KPCo's contractual netting arrangements as of March 31, 2010 and December 31, 2009:

	Liabilities of Contracts with Cross Default Provisions Prior to Contractual Netting Arrangements	Amount of Cash Collateral Posted	Additional Settlement Liability if Cross Default Provision is Triggered
		(in thousands)	
March 31, 2010	$ 43,795	$ 2,516	$ 10,614
December 31, 2009	31,000	628	7,000

7. FAIR VALUE MEASUREMENTS

The accounting guidance for "Fair Value Measurements and Disclosures" establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). Where observable inputs are available for substantially the full term of the asset or liability, the instrument is categorized in Level 2. When quoted market prices are not available, pricing may be completed using comparable securities, dealer values, operating data and general market conditions to determine fair value. Valuation models utilize various inputs such as commodity, interest rate and, to a lesser degree, volatility and credit that include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in inactive markets, market corroborated inputs (i.e. inputs derived principally from, or correlated to, observable market data) and other observable inputs for the asset or liability.

For commercial activities, exchange traded derivatives, namely futures contracts, are generally fair valued based on unadjusted quoted prices in active markets and are classified as Level 1. Level 2 inputs primarily consist of OTC broker quotes in moderately active or less active markets, as well as exchange traded contracts where there is insufficient market liquidity to warrant inclusion in Level 1. Management verifies price curves using these broker quotes and classifies these fair values within Level 2 when substantially all of the fair value can be corroborated. Management typically obtains multiple broker quotes, which are non-binding in nature but are based on recent trades in the marketplace. When multiple broker quotes are obtained, the quoted bid and ask prices are averaged. In certain circumstances, a broker quote may be discarded if it is a clear outlier. Management uses a historical correlation analysis between the broker quoted location and the illiquid locations and if the points are highly correlated, these locations are included within Level 2 as well. Certain OTC and bilaterally executed derivative instruments are executed in less active markets with a lower availability of pricing information. Long-dated and illiquid complex or structured transactions and FTRs can introduce the need for internally developed modeling inputs based upon extrapolations and assumptions of observable market data to estimate fair value. When such inputs have a significant impact on the measurement of fair value, the instrument is categorized as Level 3.

Fair Value Measurements of Long-term Debt

The fair values of Long-term Debt are based on quoted market prices, without credit enhancements, for the same or similar issues and the current interest rates offered for instruments with similar maturities. These instruments are not marked-to-market. The estimates presented are not necessarily indicative of the amounts that could be realized in a current market exchange.

The book values and fair values of KPCo's Long-term Debt as of March 31, 2010 and December 31, 2009 are summarized in the following table:

	March 31, 2010		December 31, 2009	
	Book Value	Fair Value	Book Value	Fair Value
	(in thousands)			
Long-term Debt	$ 548,763	$ 608,264	$ 548,722	$ 599,909

Fair Value Measurements of Financial Assets and Liabilities

The following tables set forth, by level within the fair value hierarchy, KPCo's financial assets and liabilities that were accounted for at fair value on a recurring basis as of March 31, 2010 and December 31, 2009. As required by the accounting guidance for "Fair Value Measurements and Disclosures," financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Management's assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels. There have not been any significant changes in management's valuation techniques.

Assets and Liabilities Measured at Fair Value on a Recurring Basis
March 31, 2010

	Level 1	Level 2	Level 3	Other	Total
Assets:			(in thousands)		
Risk Management Assets					
Risk Management Commodity Contracts (a) (d)	$ 780	$ 145,610	$ 5,886	$ (123,294)	$ 28,982
Cash Flow Hedges:					
Commodity Hedges (a)	-	1,089	-	(934)	155
Dedesignated Risk Management Contracts (b)	-	-	-	1,503	1,503
Total Risk Management Assets	$ 780	$ 146,699	$ 5,886	$ (122,725)	$ 30,640
Liabilities:					
Risk Management Liabilities					
Risk Management Commodity Contracts (a) (d)	$ 801	$ 141,677	$ 1,978	$ (132,110)	$ 12,346
Cash Flow Hedges:					
Commodity Hedges (a)	-	1,898	-	(934)	964
DETM Assignment (c)	-	-	-	381	381
Total Risk Management Liabilities	$ 801	$ 143,575	$ 1,978	$ (132,663)	$ 13,691

Assets and Liabilities Measured at Fair Value on a Recurring Basis
December 31, 2009

	Level 1	Level 2	Level 3	Other	Total
Assets:			(in thousands)		
Risk Management Assets					
Risk Management Contracts (a)	$ 472	$ 90,327	$ 2,592	$ (72,387)	$ 21,004
Cash Flow and Fair Value Hedges (a)	-	748	-	(326)	422
Dedesignated Risk Management Contracts (b)	-	-	-	1,759	1,759
Total Risk Management Assets	$ 472	$ 91,075	$ 2,592	$ (70,954)	$ 23,185
Liabilities:					
Risk Management Liabilities					
Risk Management Contracts (a)	$ 533	$ 84,831	$ 693	$ (78,030)	$ 8,027
Cash Flow and Fair Value Hedges (a)	-	1,040	-	(326)	714
DETM Assignment (c)	-	-	-	550	550
Total Risk Management Liabilities	$ 533	$ 85,871	$ 693	$ (77,806)	$ 9,291

(a) Amounts in "Other" column primarily represent counterparty netting of risk management and hedging contracts and associated cash collateral under the accounting guidance for "Derivatives and Hedging."

(b) Represents contracts that were originally MTM but were subsequently elected as normal under the accounting guidance for "Derivatives and Hedging." At the time of the normal election, the MTM value was frozen and no longer fair valued. This MTM value will be amortized into revenues over the remaining life of the contracts.

(c) See "Natural Gas Contracts with DETM" section of Note 12 in the 2009 Annual Report.

(d) Substantially comprised of power contracts.

There have been no transfers between Level 1 and Level 2 during the three months ended March 31, 2010.

The following tables set forth a reconciliation of changes in the fair value of net trading derivatives classified as level 3 in the fair value hierarchy:

Three Months Ended March 31, 2010	**Net Risk Management Assets (Liabilities)**
	(in thousands)
Balance as of January 1, 2010	$ 1,899
Realized Gain (Loss) Included in Net Income (or Changes in Net Assets) (a) (b)	1,870
Unrealized Gain (Loss) Included in Net Income (or Changes in Net Assets) Relating to Assets Still Held at the Reporting Date (a)	-
Realized and Unrealized Gains (Losses) Included in Other Comprehensive Income	-
Purchases, Issuances and Settlements (c)	(2,130)
Transfers into Level 3 (d) (h)	88
Transfers out of Level 3 (e) (h)	54
Changes in Fair Value Allocated to Regulated Jurisdictions (g)	2,128
Balance as of March 31, 2010	$ 3,908

Three Months Ended March 31, 2009	**Net Risk Management Assets (Liabilities)**
	(in thousands)
Balance as of January 1, 2009	$ 1,713
Realized (Gain) Loss Included in Net Income (or Changes in Net Assets) (a)	(834)
Unrealized Gain (Loss) Included in Net Income (or Changes in Net Assets) Relating to Assets Still Held at the Reporting Date (a)	-
Realized and Unrealized Gains (Losses) Included in Other Comprehensive Income	-
Purchases, Issuances and Settlements	-
Transfers in and/or out of Level 3 (f)	(16)
Changes in Fair Value Allocated to Regulated Jurisdictions (g)	1,528
Balance as of March 31, 2009	$ 2,391

(a) Included in revenues on KPCo's Condensed Statements of Income.
(b) Represents the change in fair value between the beginning of the reporting period and the settlement of the risk management commodity contract.
(c) Represents the settlement of risk management commodity contracts for the reporting period.
(d) Represents existing assets or liabilities that were previously categorized as Level 2.
(e) Represents existing assets or liabilities that were previously categorized as Level 3.
(f) Represents existing assets or liabilities that were either previously categorized as a higher level for which the inputs to the model became unobservable or assets and liabilities that were previously classified as level 3 for which the lowest significant input became observable during the period.
(g) Relates to the net gains (losses) of those contracts that are not reflected on KPCo's Condensed Statements of Income. These net gains (losses) are recorded as regulatory assets/liabilities.
(h) Transfers are recognized based on their value at the beginning of the reporting period that the transfer occurred.

8. INCOME TAXES

KPCo joins in the filing of a consolidated federal income tax return with its affiliates in the AEP System. The allocation of the AEP System's current consolidated federal income tax to the AEP System companies allocates the benefit of current tax losses to the AEP System companies giving rise to such losses in determining their current tax expense. The tax benefit of the Parent is allocated to its subsidiaries with taxable income. With the exception of the loss of the Parent, the method of allocation reflects a separate return result for each company in the consolidated group.

KPCo and other AEP subsidiaries are no longer subject to U.S. federal examination for years before 2001. KPCo and other AEP subsidiaries have completed the exam for the years 2001 through 2006 and have issues that are being pursued at the appeals level. The years 2007 and 2008 are currently under examination. Although the outcome of tax audits is uncertain, in management's opinion, adequate provisions for income taxes have been made for potential liabilities resulting from such matters. In addition, KPCo accrues interest on these uncertain tax positions. Management is not aware of any issues for open tax years that upon final resolution are expected to have a material adverse effect on net income.

KPCo, along with other AEP subsidiaries, files income tax returns in various state and local jurisdictions. These taxing authorities routinely examine the tax returns and KPCo and other AEP subsidiaries are currently under examination in several state and local jurisdictions. Management believes that previously filed tax returns have positions that may be challenged by these tax authorities. However, management believes that the ultimate resolution of these audits will not materially impact net income. With few exceptions, KPCo is no longer subject to state or local income tax examinations by tax authorities for years before 2000.

Federal Legislation

The Patient Protection and Affordable Care Act and the related Health Care and Education Reconciliation Act (Health Care Acts) were enacted in March 2010. The Health Care Acts amend tax rules so that the portion of employer health care costs that are reimbursed by the Medicare Part D prescription drug subsidy will no longer be deductible by the employer for federal income tax purposes effective for years beginning after December 31, 2012. Because of the loss of the future tax deduction, a reduction in the deferred tax asset related to the nondeductible OPEB liabilities accrued to date was recorded by KPCo in March 2010. This reduction, which was offset by recording net tax regulatory assets, did not materially affect KPCo's net income, cash flows or financial condition for the three months ended March 31, 2010.

9. FINANCING ACTIVITIES

Long-term Debt

KPCo did not have any long-term debt issuances or retirements during the first three months of 2010.

Utility Money Pool – AEP System

The AEP System uses a corporate borrowing program to meet the short-term borrowing needs of its subsidiaries. The corporate borrowing program includes a Utility Money Pool, which funds the utility subsidiaries. The AEP System Utility Money Pool operates in accordance with the terms and conditions approved in a regulatory order. The amount of outstanding loans (borrowings) to/from the Utility Money Pool as of March 31, 2010 and December 31, 2009 is included in Advances to/from Affiliates on KPCo's balance sheets. KPCo's Utility Money Pool activity and corresponding authorized borrowing limits for the three months ended March 31, 2010 are described in the following table:

Maximum Borrowings from Utility Money Pool	Maximum Loans to Utility Money Pool	Average Borrowings from Utility Money Pool	Average Loans to Utility Money Pool	Loans to Utility Money Pool as of March 31, 2010	Authorized Short-Term Borrowing Limit
		(in thousands)			
$ 11,883	$ 8,483	$ 3,013	$ 3,682	$ 5,817	$ 250,000

Maximum, minimum and average interest rates for funds either borrowed from or loaned to the Utility Money Pool for the three months ended March 31, 2010 and 2009 are summarized in the following table:

	Maximum Interest Rates for Funds Borrowed from the Utility Money Pool	Minimum Interest Rates for Funds Borrowed from the Utility Money Pool	Maximum Interest Rates for Funds Loaned to the Utility Money Pool	Minimum Interest Rates for Funds Loaned to the Utility Money Pool	Average Interest Rates for Funds Borrowed from the Utility Money Pool	Average Interest Rates for Funds Loaned to the Utility Money Pool
2010	0.34%	0.09%	0.17%	0.09%	0.17%	0.13%
2009	2.28%	1.22%	-%	-%	1.69%	-%

Dividend Restrictions

Federal Power Act

The Federal Power Act prohibits KPCo from participating "in the making or paying of any dividends of such public utility from any funds properly included in capital account." The term "capital account" is not defined in the Federal Power Act or its regulations. Management understands "capital account" to mean the par value of the common stock multiplied by the number of shares outstanding. This restriction does not limit the ability of KPCo to pay dividends out of retained earnings.

Leverage Restrictions

Pursuant to credit agreement leverage restrictions, as of March 31, 2010, none of the retained earnings of KPCo have restrictions related to the payment of dividends.

Credit Facilities

KPCo and certain other companies in the AEP System have a $627 million 3-year credit agreement. Under the facility, letters of credit may be issued. As of March 31, 2010, there were no outstanding amounts for KPCo under the facility.

Sale of Receivables – AEP Credit

Under a securitization arrangement, the KPCo sells, without recourse, certain of its customer accounts receivable and accrued unbilled revenue balances to AEP Credit and are charged a fee based on AEP Credit financing costs, uncollectible accounts experience for each company's receivables and administrative costs. The costs of factoring customer accounts receivable are reported in Other Operation of the participant's statement of operations. AEP Credit purchases accounts receivable through a purchase agreement with KPCo. Customer accounts receivable securitized for the electric operating companies are managed by KPCo. KPCo continues to service the receivables.

KPCo's securitized accounts receivable and accrued unbilled revenues were $44,718 thousand and $41,295 thousand as of March 31, 2010 and December 31, 2009, respectively.

KPCo paid fees to AEP Credit for factoring customer accounts receivable of $628 thousand for the three months ended March 31, 2010.

KPCo's proceeds on the sale of receivables to AEP Credit for the three month ended March 31, 2010 was $145,724 thousand.

10. COMPANY-WIDE STAFFING AND BUDGET REVIEW

In April 2010, management began initiatives to decrease both labor and non-labor expenditures with a goal of achieving significant reductions in operation and maintenance expenses. One initiative is to offer a one-time voluntary severance program. Participating employees will receive two weeks of base pay for every year of service. It is anticipated that more than 2,000 employees will accept voluntary severances and terminate employment no later than May 2010. The second simultaneous initiative will involve all business units and departments to identify process improvements, streamlined organizational designs and other efficiencies that can deliver additional lasting savings. There is the potential that actions taken as a result of this effort could lead to some involuntary separations. Affected employees would receive the same severance package as those who volunteered.

Management expects to record a charge to expense in the second quarter of 2010 related to these initiatives. At this time, management is unable to predict the impact of these initiatives on net income, cash flows and financial condition.