

AEP Generating Company

2019 First Quarter Report

Financial Statements



BOUNDLESS ENERGYSM

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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	American Electric Power Company, Inc., an investor-owned electric public utility holding company which includes American Electric Power Company, Inc. (Parent) and majority owned consolidated subsidiaries and consolidated affiliates.
AEP System	American Electric Power System, an electric system, owned and operated by AEP subsidiaries.
ASU	Accounting Standards Update.
Excess ADIT	Excess accumulated deferred income taxes.
FASB	Financial Accounting Standards Board.
FERC	Federal Energy Regulatory Commission.
GAAP	Accounting Principles Generally Accepted in the United States of America.
I&M	Indiana Michigan Power Company, an AEP electric utility subsidiary.
IRS	Internal Revenue Service.
KPCo	Kentucky Power Company, an AEP electric utility subsidiary.
MW	Megawatt.
NSR	New Source Review.
OPEB	Other Postretirement Benefits.
Parent	American Electric Power Company, Inc., the equity owner of AEP subsidiaries within the AEP consolidation.
Rockport Plant	A generation plant, consisting of two 1,310 MW coal-fired generating units near Rockport, Indiana. AEGCo and I&M jointly-own Unit 1. In 1989, AEGCo and I&M entered into a sale-and-leaseback transaction with Wilmington Trust Company, an unrelated, unconsolidated trustee for Rockport Plant, Unit 2.
UMWA	United Mine Workers of America.
Utility Money Pool	Centralized funding mechanism AEP uses to meet the short-term cash requirements of certain utility subsidiaries.

AEP GENERATING COMPANY
CONDENSED STATEMENTS OF INCOME
For the Three Months Ended March 31, 2019 and 2018
(in thousands)
(Unaudited)

	Three Months Ended March 31,	
REVENUES	2019	2018
Sales to AEP Affiliates	\$ 82,204	\$ 87,708
Other Revenues – Affiliated	4,046	4,637
Other Revenues – Nonaffiliated	85	994
TOTAL REVENUES	86,335	93,339
EXPENSES		
Fuel and Other Consumables Used for Electric Generation	37,402	46,131
Rent – Rockport Plant, Unit 2	16,835	17,071
Other Operation	5,854	6,334
Maintenance	5,885	5,619
Depreciation and Amortization	15,655	11,459
Taxes Other Than Income Taxes	1,454	1,198
TOTAL EXPENSES	83,085	87,812
OPERATING INCOME	3,250	5,527
Other Income (Expense):		
Other Income	534	548
Non-Service Cost Components of Net Periodic Benefit Cost	294	261
Interest Expense	(1,534)	(1,100)
INCOME BEFORE INCOME TAX EXPENSE (BENEFIT)	2,544	5,236
Income Tax Expense (Benefit)	(834)	676
NET INCOME	\$ 3,378	\$ 4,560

The common stock of AEGCo is wholly-owned by Parent.

See Condensed Notes to Condensed Financial Statements beginning on page 7.

AEP GENERATING COMPANY
CONDENSED STATEMENTS OF CHANGES IN
COMMON SHAREHOLDER'S EQUITY
For the Three Months Ended March 31, 2019 and 2018
(in thousands)
(Unaudited)

	<u>Common Stock</u>	<u>Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Total</u>
TOTAL COMMON SHAREHOLDER'S EQUITY – DECEMBER 31, 2017	\$ 1,000	\$ 175,487	\$ 94,475	\$ 270,962
Net Income			4,560	4,560
TOTAL COMMON SHAREHOLDER'S EQUITY – MARCH 31, 2018	<u>\$ 1,000</u>	<u>\$ 175,487</u>	<u>\$ 99,035</u>	<u>\$ 275,522</u>
TOTAL COMMON SHAREHOLDER'S EQUITY – DECEMBER 31, 2018	\$ 1,000	\$ 165,487	\$ 54,913	\$ 221,400
Net Income			3,378	3,378
TOTAL COMMON SHAREHOLDER'S EQUITY – MARCH 31, 2019	<u>\$ 1,000</u>	<u>\$ 165,487</u>	<u>\$ 58,291</u>	<u>\$ 224,778</u>

See Condensed Notes to Condensed Financial Statements beginning on page 7.

AEP GENERATING COMPANY
CONDENSED BALANCE SHEETS
ASSETS
March 31, 2019 and December 31, 2018
(in thousands)
(Unaudited)

	March 31, 2019	December 31, 2018
CURRENT ASSETS		
Advances to Affiliates	\$ 93,476	\$ 70,904
Accounts Receivable:		
Customers	7	466
Affiliated Companies	30,773	30,196
Total Accounts Receivable	<u>30,780</u>	<u>30,662</u>
Fuel	32,040	37,289
Materials and Supplies	18,375	18,062
Prepayments and Other Current Assets	4,173	2,128
TOTAL CURRENT ASSETS	<u>178,844</u>	<u>159,045</u>
PROPERTY, PLANT AND EQUIPMENT		
Electric Generation	1,125,626	1,125,208
Other Property, Plant and Equipment	35,946	35,564
Construction Work in Progress	60,447	50,525
Total Property, Plant and Equipment	<u>1,222,019</u>	<u>1,211,297</u>
Accumulated Depreciation and Amortization	735,617	719,684
TOTAL PROPERTY, PLANT AND EQUIPMENT – NET	<u>486,402</u>	<u>491,613</u>
OTHER NONCURRENT ASSETS		
Regulatory Assets	14,480	14,671
Operating Lease Assets	270,208	—
Deferred Charges and Other Noncurrent Assets	4,524	1,871
TOTAL OTHER NONCURRENT ASSETS	<u>289,212</u>	<u>16,542</u>
TOTAL ASSETS	<u>\$ 954,458</u>	<u>\$ 667,200</u>

See Condensed Notes to Condensed Financial Statements beginning on page 7.

AEP GENERATING COMPANY
CONDENSED BALANCE SHEETS
LIABILITIES AND COMMON SHAREHOLDER'S EQUITY
March 31, 2019 and December 31, 2018
(Unaudited)

	March 31, 2019	December 31, 2018
CURRENT LIABILITIES		
(in thousands)		
Accounts Payable:		
General	\$ 2,346	\$ 2,151
Affiliated Companies	19,618	23,250
Long-term Debt Due Within One Year – Nonaffiliated	45,000	45,000
Accrued Taxes	11,981	6,451
Accrued Rent – Rockport Plant, Unit 2	2,703	4,963
Obligations Under Operating Leases	69,514	—
Other Current Liabilities	3,030	3,463
TOTAL CURRENT LIABILITIES	154,192	85,278
NONCURRENT LIABILITIES		
Long-term Debt – Nonaffiliated	149,988	149,988
Deferred Income Taxes	29,568	30,872
Regulatory Liabilities and Deferred Investment Tax Credits	106,587	90,008
Deferred Gain on Sale-and-Leaseback – Rockport Plant, Unit 2	—	21,911
Obligations Under Operating Leases	220,257	—
Deferred Credits and Other Noncurrent Liabilities	69,088	67,743
TOTAL NONCURRENT LIABILITIES	575,488	360,522
TOTAL LIABILITIES	729,680	445,800
Commitments and Contingencies (Note 3)		
COMMON SHAREHOLDER'S EQUITY		
Common Stock – Par Value – \$1,000 Per Share:		
Authorized – 1,000 Shares		
Outstanding – 1,000 Shares	1,000	1,000
Paid-in Capital	165,487	165,487
Retained Earnings	58,291	54,913
TOTAL COMMON SHAREHOLDER'S EQUITY	224,778	221,400
TOTAL LIABILITIES AND COMMON SHAREHOLDER'S EQUITY	\$ 954,458	\$ 667,200

See Condensed Notes to Condensed Financial Statements beginning on page 7.

AEP GENERATING COMPANY
CONDENSED STATEMENTS OF CASH FLOWS
For the Three Months Ended March 31, 2019 and 2018
(in thousands)
(Unaudited)

	Three Months Ended March 31,	
	2019	2018
OPERATING ACTIVITIES		
Net Income	\$ 3,378	\$ 4,560
Adjustments to Reconcile Net Income to Net Cash Flows from Operating Activities:		
Depreciation and Amortization	15,655	11,459
Deferred Income Taxes	(2,842)	(210)
Amortization of Deferred Gain on Sale-and-Leaseback – Rockport Plant, Unit 2	(1,393)	(1,393)
Allowance for Equity Funds Used During Construction	41	35
Change in Other Noncurrent Assets	(1,577)	(1,842)
Change in Other Noncurrent Liabilities	156	(110)
Changes in Certain Components of Working Capital:		
Accounts Receivable	(118)	6,285
Fuel, Materials and Supplies	4,936	(3,926)
Accounts Payable	(3,573)	1,497
Accrued Taxes, Net	5,530	4,706
Accrued Rent – Rockport Plant, Unit 2	18,228	18,464
Other Current Assets	(2,055)	(744)
Other Current Liabilities	(2,400)	(814)
Net Cash Flows from Operating Activities	<u>33,966</u>	<u>37,967</u>
INVESTING ACTIVITIES		
Construction Expenditures	(11,074)	(3,718)
Change in Advances to Affiliates, Net	(22,572)	(33,928)
Other Investing Activities	—	(15)
Net Cash Flows Used for Investing Activities	<u>(33,646)</u>	<u>(37,661)</u>
FINANCING ACTIVITIES		
Principal Payments for Finance Lease Obligations	(330)	(322)
Other Financing Activities	10	16
Net Cash Flows Used for Financing Activities	<u>(320)</u>	<u>(306)</u>
Net Change in Cash and Cash Equivalents	—	—
Cash and Cash Equivalents at Beginning of Period	—	—
Cash and Cash Equivalents at End of Period	<u>\$ —</u>	<u>\$ —</u>
SUPPLEMENTARY INFORMATION		
Cash Paid for Interest, Net of Capitalized Amounts	\$ 1,349	\$ 950
Net Cash Paid for Income Taxes	82	—
Noncash Acquisitions Under Finance Leases	15	25
Construction Expenditures Included in Current Liabilities as of March 31,	253	114

See Condensed Notes to Condensed Financial Statements beginning on page 7.

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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. Net income for the three months ended March 31, 2019 is not necessarily indicative of results that may be expected for the year ending December 31, 2019. The condensed financial statements are unaudited and should be read in conjunction with the audited 2018 financial statements and notes thereto, which are included in AEGCo's 2018 Annual Report.

Subsequent Events

Management reviewed subsequent events through April 25, 2019, the date that the first quarter 2019 report was available to be issued.

2. NEW ACCOUNTING PRONOUNCEMENTS

During FASB's standard-setting process and upon issuance of final pronouncements, management reviews the new accounting literature to determine its relevance, if any, to AEGCo's business. The following pronouncements will impact the financial statements.

ASU 2016-02 "Accounting for Leases" (ASU 2016-02)

In February 2016, the FASB issued ASU 2016-02 increasing the transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheets and disclosing key information about leasing arrangements. Under the new standard, an entity must recognize an asset and liability for operating leases on the balance sheets. Additionally, a capital lease will be known as a finance lease going forward. Leases with terms of 12 months or longer will be subject to the new requirements. Fundamentally, the criteria used to determine lease classification will remain the same, but will be more subjective under the new standard.

New leasing standard implementation activities included the identification of the lease population within the AEP System as well as the sampling of representative lease contracts to analyze accounting treatment under the new accounting guidance. Based upon the completed assessments, management also prepared a gap analysis to outline new disclosure compliance requirements.

Management adopted ASU 2016-02 effective January 1, 2019 by means of a cumulative-effect adjustment to the balance sheet. Management elected the following practical expedients upon adoption:

Practical Expedient	Description
Overall Expedients (for leases commenced prior to adoption date and must be adopted as a package)	Do not need to reassess whether any expired or existing contracts are/or contain leases, do not need to reassess the lease classification for any expired or existing leases and do not need to reassess initial direct costs for any existing leases.
Lease and Non-lease Components (elect by class of underlying asset)	Elect as an accounting policy to not separate non-lease components from lease components and instead account for each lease and associated non-lease component as a single lease component.
Short-term Lease (elect by class of underlying asset)	Elect as an accounting policy to not apply the recognition requirements to short-term leases.
Existing and expired land easements not previously accounted for as leases	Elect optional transition practical expedient to not evaluate under Topic 842 existing or expired land easements that were not previously accounted for as leases under the current leases guidance in Topic 840.
Cumulative-effect adjustment in the period of adoption	Elect the optional transition practical expedient to adopt the new lease requirements through a cumulative-effect adjustment on the balance sheet in the period of adoption.

Management concluded that the result of adoption would not materially change the volume of contracts that qualify as leases going forward. The adoption of the new standard did not materially impact results of operations or cash flows, but did have a material impact on the balance sheet. See Note 7 - Leases for additional disclosures required by the new standard.

ASU 2016-13 "Measurement of Credit Losses on Financial Instruments" (ASU 2016-13)

In June 2016, the FASB issued ASU 2016-13 requiring an allowance to be recorded for all expected credit losses for financial assets. The allowance for credit losses is based on historical information, current conditions and reasonable and supportable forecasts. The new standard also makes revisions to the other-than-temporary impairment model for available-for-sale debt securities. Disclosures of credit quality indicators in relation to the amortized cost of financing receivables are further disaggregated by year of origination.

The new accounting guidance is effective for interim and annual periods beginning after December 15, 2020, with early adoption permitted for interim and annual periods beginning after December 15, 2018. The amendments will be applied through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective. Management is analyzing the impact of this new standard and, at this time, cannot estimate the impact of adoption on net income. Management plans to adopt ASU 2016-13 and related implementation guidance effective January 1, 2020.

ASU 2018-15 “Internal-Use Software: Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract” (ASU 2018-15)

In August 2018, the FASB issued ASU 2018-15 aligning the requirements for capitalizing implementation costs incurred in a cloud computing arrangement (hosting arrangement) that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. The new standard requires an entity (customer) in a hosting arrangement that is a service contract to follow the accounting guidance for “Internal-Use Software” to determine which implementation costs to capitalize as an asset related to the service contract and which costs to expense. To eliminate diversity in practice, the new standard changes the presentation of implementation costs for cloud service arrangements that are service contracts without the purchase of a license. Implementation costs for cloud service contracts will be presented on the balance sheets in the same manner as a prepayment. AEGCo currently presents implementation costs in property, plant and equipment on the balance sheets. Under the new standard, amortization of capitalized implementation costs of a hosting arrangement will be recorded in Operation and Maintenance expense over the term of the cloud service arrangement, rather than Depreciation and Amortization expense on the statements of income. Payments for capitalized implementation costs in the statement of cash flows will be classified in the same manner as payments made for fees associated with the hosting element.

The new accounting guidance is effective for interim and annual periods beginning after December 15, 2020, with early adoption permitted. The amendments may be applied either retrospectively or prospectively to applicable implementation costs incurred after the date of adoption. Management is analyzing the impact of this new standard and at this time, cannot estimate the impact of adoption on results of operations, financial position or cash flows. Management plans to adopt ASU 2018-15 prospectively, effective January 1, 2020.

3. COMMITMENTS, GUARANTEES AND CONTINGENCIES

AEGCo is subject to certain claims and legal actions arising in its ordinary course of business. In addition, AEGCo'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 against AEGCo cannot be predicted. Management accrues contingent liabilities only when management concludes that it is both probable that a liability has been incurred at the date of the financial statements and the amount of loss can be reasonably estimated. When management determines that it is not probable, but rather reasonably possible that a liability has been incurred at the date of the financial statements, management discloses such contingencies and the possible loss or range of loss if such estimate can be made. Any estimated range is based on currently available information and involves elements of judgment and significant uncertainties. Any estimated range of possible loss may not represent the maximum possible loss exposure. Circumstances change over time and actual results may vary significantly from estimates.

For current proceedings not specifically discussed below, management does not anticipate that the liabilities, if any, arising from such proceedings would have a material effect on the financial statements. The Commitments, Guarantees and Contingencies note within AEGCo's 2018 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 unless specified below.

Letters of Credit

AEGCo has \$45 million of variable rate Pollution Control Bonds supported by \$45.5 million of bilateral letters of credit maturing in July 2019.

Indemnifications and Other Guarantees

Contracts

AEGCo 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. As of March 31, 2019, there were no material liabilities recorded for any indemnifications.

CONTINGENCIES

Rockport Plant Litigation

In 2013, the Wilmington Trust Company filed a complaint in the U.S. District Court for the Southern District of New York against AEGCo and I&M alleging that it would be unlawfully burdened by the terms of the modified NSR consent decree after the Rockport Plant, Unit 2 lease expiration in December 2022. The terms of the consent decree allow the installation of environmental emission control equipment, repowering, refueling or retirement of the unit. The plaintiffs seek a judgment declaring that the defendants breached the lease, must satisfy obligations related to installation of emission control equipment and indemnify the plaintiffs. The New York court granted a motion to transfer this case to the U.S. District Court for the Southern District of Ohio.

AEGCo and I&M sought and were granted dismissal by the U.S. District Court for the Southern District of Ohio of certain of the plaintiffs' claims, including claims for compensatory damages, breach of contract, breach of the implied covenant of good faith and fair dealing and indemnification of costs. Plaintiffs voluntarily dismissed the surviving claims that AEGCo and I&M failed to exercise prudent utility practices with prejudice, and the court issued a final judgment. The plaintiffs subsequently filed an appeal in the U.S. Court of Appeals for the Sixth Circuit.

In 2017, the U.S. Court of Appeals for the Sixth Circuit issued an opinion and judgment affirming the district court's dismissal of the owners' breach of good faith and fair dealing claim as duplicative of the breach of contract claims reversing the district court's dismissal of the breach of contract claims, and remanding the case for further proceedings.

Thereafter, AEP filed a motion with the U.S. District Court for the Southern District of Ohio in the original NSR litigation, seeking to modify the consent decree. The district court granted the owners' unopposed motion to stay the lease litigation to afford time for resolution of AEP's motion to modify the consent decree. In September 2018, the district court granted AEP's unopposed motion to stay further proceedings regarding the consent decree to facilitate settlement discussions among the parties to the consent decree.

Management will continue to defend against the claims. Given that the district court dismissed plaintiffs' claims seeking compensatory relief as premature, and that plaintiffs have yet to present a methodology for determining or any analysis supporting any alleged damages, management is unable to determine a range of potential losses that are reasonably possible of occurring.

4. BENEFIT PLANS

AEGCo participates in an AEP sponsored qualified pension plan. Substantially all of AEGCo's employees who are not UMWA members are covered by the qualified plan. AEGCo also participates in OPEB plans sponsored by AEP to provide health and life insurance benefits for retired employees.

Components of Net Periodic Benefit Cost

The following table provides the components of AEGCo's net periodic benefit cost (credit) for the plans:

	Pension Plan		OPEB	
	Three Months Ended March 31, 2019	2018	Three Months Ended March 31, 2019	2018
	(in thousands)			
Service Cost	\$ 23	\$ 21	\$ 202	\$ 291
Interest Cost	31	30	508	504
Expected Return on Plan Assets	(67)	(64)	(622)	(685)
Amortization of Prior Service Credit	—	—	(17)	(17)
Amortization of Net Actuarial Loss	8	13	99	180
Net Periodic Benefit Cost (Credit)	\$ (5)	\$ —	\$ 170	\$ 273

5. FAIR VALUE MEASUREMENTS

Fair Value Hierarchy and Valuation Techniques

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.

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 classified as Level 2 measurement inputs. 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 AEGCo’s Long-term Debt are summarized in the following table:

	March 31, 2019		December 31, 2018	
	Book Value	Fair Value	Book Value	Fair Value
	(in thousands)			
Long-term Debt	\$ 194,988	\$ 195,000	\$ 194,988	\$ 195,000

6. INCOME TAXES

Effective Tax Rates (ETR)

The interim ETR for AEGCo reflects the estimated annual ETR for 2019 and 2018, adjusted for tax expense associated with certain discrete items. The interim ETR of (32.8)% and 12.9% in 2019 and 2018, respectively, differs from the federal statutory tax rate of 21% primarily due to state income taxes, amortization of Excess ADIT, tax credits and other book/tax differences which are accounted for on a flow-through basis.

Three Months Ended March 31, 2019 Compared to Three Months Ended March 31, 2018

The decrease in ETR was primarily due to \$865 thousand of increased amortization of Excess ADIT which impacted the ETR by (35.9)%. The increased amortization of Excess ADIT was primarily driven by the acceleration in the expected retirement dates of Rockport, Unit 1 from 2044 to 2028. Additionally, the ETR decreased as a result of an increase in parent company loss benefit, a decrease in state income taxes, and an increase in tax credits which impacted the ETR by (4.2)%, (2.7)% and (2.3)%, respectively.

Federal and State Income Tax Audit Status

The IRS has completed its examination of AEGCo and other AEP subsidiaries for all years through 2016.

AEGCo and other AEP subsidiaries file income tax returns in various state and local jurisdictions. These taxing authorities routinely examine the tax returns. AEGCo and other AEP subsidiaries are currently under examination in several state and local jurisdictions. However, it is possible that previously filed tax returns have positions that may be challenged by these tax authorities. Management believes that adequate provisions for income taxes have been made for potential liabilities resulting from such challenges and that the ultimate resolution of these audits will not materially impact net income. AEGCo is no longer subject to state, local or non-U.S. income tax examinations by tax authorities for years before 2007.

7. LEASES

AEGCo leases property, plant and equipment including, but not limited to, fleet, information technology and real estate leases. These leases require payments of non-lease components, including related property taxes, operating and maintenance costs. As of the adoption date of ASU 2016-02, management elected not to separate non-lease components from associated lease components in accordance with the accounting guidance for “Leases.” Many of these leases have purchase or renewal options. Leases not renewed are often replaced by other leases. Options to renew or purchase a lease are included in the measurement of lease assets and liabilities if it is reasonably certain that AEGCo will exercise the option.

Lease obligations are measured using the rate implicit in the lease when that rate is readily determinable. When the implicit rate is not readily determinable, AEGCo calculates its lease obligation using its incremental borrowing rate. Spreads to estimate the discount associated with borrowing on a secured basis are incorporated into the calculation.

Lease rentals for both operating and finance leases are generally charged to Other Operation and Maintenance expense in accordance with rate-making treatment for regulated operations. Additionally, for regulated operations with finance leases, a finance lease asset and offsetting liability are recorded at the present value of the remaining lease payments for each reporting period. Finance leases for nonregulated property are accounted for as if the assets were owned and financed. The components of rental costs were as follows:

Lease Rental Costs	Three Months Ended March 31, 2019
	(in thousands)
Operating Lease Cost	\$ 19,367
Amortization of Finance Leases	448
Interest on Finance Leases	359
Total Lease Rental Costs (a)	\$ 20,174

- (a) Excludes variable and short-term lease costs, which were immaterial for the three months ended March 31, 2019.

Supplemental information related to leases as of and for the three months ended March 31, 2019 are shown in the tables below.

Lease Type	Weighted-Average Remaining Lease Term (years):	Weighted-Average Discount Rate
Operating Leases	3.84	3.49%
Finance Leases	4.24	4.68%

	Three Months Ended March 31, 2019
	(in thousands)
Cash paid for amounts included in the measurement of lease liabilities:	
Operating Cash Flows from Operating Leases	\$ 1,836
Operating Cash Flows from Finance Leases	254
Financing Cash Flows from Finance Leases	330
Non-cash Acquisitions Under Operating Leases	\$ —

The following tables show the property, plant and equipment under finance leases and noncurrent assets under operating leases and related obligations recorded on AEGCo's balance sheets. Unless shown as a separate line on the balance sheets due to materiality, net operating lease assets are included in Deferred Charges and Other Noncurrent Assets, current finance lease obligations are included in Other Current Liabilities and long-term finance lease obligations are included in Deferred Credits and Other Noncurrent Liabilities on AEGCo's balance sheets. Lease obligations are not recognized on the balance sheets for lease agreements with a lease term of less than twelve months.

	<u>March 31, 2019</u> <u>(in thousands)</u>
Property, Plant and Equipment Under Finance Leases	
Generation	\$ 25,309
Other Property, Plant and Equipment	1,510
Total Property, Plant and Equipment Under Capital Leases	<u>26,819</u>
Accumulated Amortization	8,987
Net Property, Plant and Equipment Under Finance Leases	<u><u>\$ 17,832</u></u>
Obligations Under Finance Leases	
Noncurrent Liability	\$ 16,063
Liability Due Within One Year	1,769
Total Obligations Under Finance Leases	<u><u>\$ 17,832</u></u>
Operating Lease Assets	
	<u><u>\$ 270,208</u></u>
Obligations Under Operating Leases	
Noncurrent Liability	\$ 220,257
Liability Due Within One Year	69,514
Total Obligations Under Operating Leases	<u><u>\$ 289,771</u></u>

Future minimum lease payments as of March 31, 2019 are presented on a rolling 12-month basis as shown in the table below:

<u>Future Minimum Lease Payments</u>	<u>Finance Leases</u>	<u>Noncancelable Operating Leases</u>
	<u>(in thousands)</u>	
Year 1	\$ 3,247	\$ 78,414
Year 2	3,231	78,206
Year 3	3,138	77,988
Year 4	3,057	77,438
Year 5	2,960	336
Later Years	8,019	12
Total Future Minimum Lease Payments	<u>23,652</u>	<u>312,394</u>
Less Imputed Interest	5,820	22,623
Estimated Present Value of Future Minimum Lease Payments	<u><u>\$ 17,832</u></u>	<u><u>\$ 289,771</u></u>

Future minimum lease payments consisted of the following as of December 31, 2018:

<u>Future Minimum Lease Payments</u>	<u>Finance Leases</u>	<u>Noncancelable Operating Leases</u>
	(in thousands)	
2019	\$ 3,240	\$ 78,415
2020	3,230	78,309
2021	3,169	77,993
2022	3,074	77,968
2023	2,964	336
Later Years	8,524	13
Total Future Minimum Lease Payments	<u>24,201</u>	<u>\$ 313,034</u>
Less Imputed Interest	5,936	
Estimated Present Value of Future Minimum Lease Payments	<u>\$ 18,265</u>	

Master Lease Agreements

AEGCo leases certain equipment under master lease agreements. Under the lease agreements, the lessor is guaranteed a residual value up to a stated percentage of 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, AEGCo is committed to pay the difference between the actual fair value and the residual value guarantee. Historically, at the end of the lease term the fair value has been in excess of the amount guaranteed. As of March 31, 2019, the maximum potential loss for these lease agreements was \$36 thousand assuming the fair value of the equipment is zero at the end of the lease term.

Rockport Lease

AEGCo and I&M entered into a sale-and-leaseback transaction in 1989 with Wilmington Trust Company (Owner Trustee), an unrelated, unconsolidated trustee for Rockport Plant, Unit 2 (the Plant). The Owner Trustee was capitalized with equity from six owner participants with no relationship to AEP or any of its subsidiaries and debt from a syndicate of banks and securities in a private placement to certain institutional investors. In the first quarter of 2019, in accordance with ASU 2016-02, the \$21.9 million unamortized gain associated with the sale-and-leaseback of the Plant was recognized as an adjustment to equity. The adjustment to equity was then reclassified to regulatory liabilities in accordance with accounting guidance for “Regulated Operations” as AEGCo and I&M will continue to provide the benefit of the unamortized gain to customers in future periods.

The Owner Trustee owns the Plant and leases it equally to AEGCo and I&M. The lease is accounted for as an operating lease with the payment obligations included in the future minimum lease payments schedule earlier in this note. The lease term is for 33 years with potential renewal options. At the end of the lease term, AEGCo and I&M have the option to renew the lease at a rate that approximates fair value. The option to renew was not included in the measurement of the lease obligation as of March 31, 2019 as the option to renew was not reasonably certain. AEP, AEGCo and I&M have no ownership interest in the Owner Trustee and do not guarantee its debt. AEGCo’s future minimum lease payments for this sale-and-leaseback transaction as of March 31, 2019 were as follows:

<u>Future Minimum Lease Payments</u>	<u>(in thousands)</u>
2019	\$ 73,854
2020	73,854
2021	73,854
2022	73,854
Total Future Minimum Lease Payments	<u>\$ 295,416</u>

Lessor Activity

AEGCo’s lessor activity was immaterial as of and for the three months ended March 31, 2019.

8. FINANCING ACTIVITIES

Long-term Debt

AEGCo did not have any long-term debt issuances or retirements during the first three months of 2019.

Dividend Restrictions

AEGCo pays dividends to Parent provided funds are legally available. Various financing arrangements may impose certain restrictions on the ability of AEGCo to transfer funds to Parent in the form of dividends.

AEGCo has credit agreements that contain a covenant that limit its debt to capitalization ratio to 67.5%. As of March 31, 2019, AEGCo did not exceed its debt to capitalization limit. The method for calculating outstanding debt and capitalization is contractually-defined in the credit agreements.

Corporate Borrowing Program – AEP System

The AEP System uses a corporate borrowing program to meet the short-term borrowing needs of AEP's subsidiaries. The corporate borrowing program includes a Utility Money Pool, which funds AEP's utility subsidiaries. The AEP System Utility Money Pool operates in accordance with the terms and conditions of the AEP System Utility Money Pool agreement filed with the FERC. The amounts of outstanding loans to the Utility Money Pool as of March 31, 2019 and December 31, 2018 are included in Advances to Affiliates on AEGCo's balance sheets. AEGCo's Utility Money Pool activity and corresponding authorized borrowing limits for the three months ended March 31, 2019 are described in the following table:

Maximum Loans to the Utility Money Pool	Average Loans to the Utility Money Pool	Loans to the Utility Money Pool as of March 31, 2019	Authorized Short-Term Borrowing Limit
(in thousands)			
\$ 95,744	\$ 82,425	\$ 93,476	\$ 200,000

Maximum, minimum and average interest rates for funds loaned to the Utility Money Pool are summarized in the following table:

Three Months Ended March 31,	Maximum Interest Rate for Funds Loaned to the Utility Money Pool	Minimum Interest Rate for Funds Loaned to the Utility Money Pool	Average Interest Rate for Funds Loaned to the Utility Money Pool
2019	3.02%	2.73%	2.86%
2018	2.42%	1.83%	2.01%

9. REVENUE FROM CONTRACTS WITH CUSTOMERS

Disaggregated Revenues from Contracts with Customers

AEGCo's statements of income represent revenues from contracts with customers by type of revenue. AEGCo did not have alternative revenues for March 31, 2019 and March 31, 2018.

Fixed Performance Obligations

As of March 31, 2019, there are no fixed performance obligations related to AEGCo.

Contract Assets and Liabilities

Contract assets are recognized when AEGCo has a right to consideration that is conditional upon the occurrence of an event other than the passage of time, such as future performance under a contract. AEGCo did not have any material contract assets as of March 31, 2019 and December 31, 2018.

When AEGCo receives consideration, or such consideration is unconditionally due from a customer prior to transferring goods or services to the customer under the terms of a sales contract, they recognize a contract liability on the balance sheet in the amount of that consideration. Revenue for such consideration is subsequently recognized in the period or periods in which the remaining performance obligations in the contract are satisfied. AEGCo did not have any material contract liabilities as of March 31, 2019 and December 31, 2018.

Accounts Receivable from Contracts with Customers

Accounts receivable from contracts with customers are presented on AEGCo's balance sheets within the Accounts Receivable - Customers and Accounts Receivable - Affiliated Companies line items. AEGCo's balances for receivables from contracts that are not recognized in accordance with the accounting guidance for "Revenue from Contracts with Customers" included in Accounts Receivable - Customers and Accounts Receivable - Affiliated Companies are not material as of March 31, 2019 and December 31, 2018.