Kentucky Power Company

2023 Third Quarter Report

Financial Statements

KENTUCKY POWER

An AEP Company

BOUNDLESS ENERGY

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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 Credit	AEP Credit, Inc., a consolidated variable interest entity of AEP which securitizes accounts receivable and accrued utility revenues for affiliated electric utility companies.
AEP System	American Electric Power System, an electric system, owned and operated by AEP subsidiaries.
AEPSC	American Electric Power Service Corporation, an AEP service subsidiary providing management and professional services to AEP and its subsidiaries.
AEPTCo	AEP Transmission Company, LLC, a wholly-owned subsidiary of AEP Transmission Holdco, is an intermediate holding company that owns the State Transcos.
AFUDC	Allowance for Equity Funds Used During Construction.
AOCI	Accumulated Other Comprehensive Income.
APCo	Appalachian Power Company, an AEP electric utility subsidiary.
Excess ADIT	Excess accumulated deferred income taxes.
FASB	Financial Accounting Standards Board.
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.
IRA	On August 16, 2022 President Biden signed into law legislation commonly referred to as the “Inflation Reduction Act” (IRA).
IRS	Internal Revenue Service.
ITC	Investment Tax Credit.
KPCo	Kentucky Power Company, an AEP electric utility subsidiary.
KPSC	Kentucky Public Service Commission.
KTCo	AEP Kentucky Transmission Company, Inc., an affiliate of KPCo and a wholly-owned subsidiary of AEP.
MMBtu	Million British Thermal Units.
MTM	Mark-to-Market.
MW	Megawatt.
MWh	Megawatt-hour.
OPEB	Other Postretirement Benefits.
OTC	Over-the-counter.
Parent	American Electric Power Company, Inc., the equity owner of AEP subsidiaries within the AEP consolidation.
PJM	Pennsylvania – New Jersey – Maryland regional transmission organization.
PTC	Production Tax Credit.

Term	Meaning
Risk Management Contracts	Trading and non-trading derivatives, including those derivatives designated as cash flow and fair value hedges.
RPM	Reliability Pricing Model.
ROE	Return on Equity.
Rockport Plant	A generation plant, jointly owned by AEGCo and I&M, consisting of two 1,310 MW coal-fired generating units near Rockport, Indiana.
Tax Reform	On December 22, 2017, President Trump signed into law legislation referred to as the “Tax Cuts and Jobs Act” (the TCJA). The TCJA includes significant changes to the Internal Revenue Code of 1986, including a reduction in the corporate federal income tax rate from 35% to 21% effective January 1, 2018.
Utility Money Pool	Centralized funding mechanism AEP uses to meet the short-term cash requirements of certain utility subsidiaries.
WPCo	Wheeling Power Company, an AEP electric utility subsidiary.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF INCOME
For the Three and Nine Months Ended September 30, 2023 and 2022
(in thousands)
(Unaudited)

	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
REVENUES				
Electric Generation, Transmission and Distribution	$ 153,415	$ 191,639	$ 455,590	$ 544,489
Sales to AEP Affiliates	3,275	5,215	10,712	18,313
Other Revenues	189	310	609	1,325
TOTAL REVENUES	156,879	197,164	466,911	564,127
EXPENSES				
Purchased Electricity, Fuel and Other Consumables Used for Electric Generation	56,920	67,044	177,678	178,224
Purchased Electricity from AEP Affiliates	226	29,076	1,742	79,099
Other Operation	27,673	31,286	84,763	93,107
Maintenance	15,792	13,269	49,476	44,120
Depreciation and Amortization	29,476	31,458	93,501	92,116
Taxes Other Than Income Taxes	3,560	6,865	20,201	20,215
TOTAL EXPENSES	133,647	178,998	427,361	506,881
OPERATING INCOME	23,232	18,166	39,550	57,246
Other Income (Expense):				
Interest Income	12	115	69	118
Allowance for Equity Funds Used During Construction	101	248	586	646
Non-Service Cost Components of Net Periodic Benefit Cost	1,894	1,622	5,682	4,867
Interest Expense	(17,271)	(11,713)	(48,477)	(31,728)
INCOME (LOSS) BEFORE INCOME TAX BENEFIT	7,968	8,438	(2,590)	31,149
Income Tax Benefit	(6,152)	(3,157)	(23,235)	(19,534)
NET INCOME	$ 14,120	$ 11,595	$ 20,645	$ 50,683

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

See Condensed Notes to Condensed Financial Statements beginning on page 9.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
For the Three and Nine Months Ended September 30, 2023 and 2022
(in thousands)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2023	2022	2023	2022
Net Income	$ 14,120	$ 11,595	$ 20,645	$ 50,683
OTHER COMPREHENSIVE LOSS, NET OF TAXES				
Amortization of Pension and OPEB Deferred Costs, Net of Tax of $0 and $(444) for the Three Months Ended September 30, 2023 and 2022, Respectively, and $0 and $(465) for the Nine Months Ended September 30, 2023 and 2022, Respectively	—	(1,670)	—	(1,749)
TOTAL COMPREHENSIVE INCOME	$ 14,120	$ 9,925	$ 20,645	$ 48,934

See Condensed Notes to Condensed Financial Statements beginning on page 9.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF CHANGES IN
COMMON SHAREHOLDER'S EQUITY
For the Nine Months Ended September 30, 2023 and 2022
(in thousands)
(Unaudited)

	Common Stock	Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
TOTAL COMMON SHAREHOLDER'S EQUITY - DECEMBER 31, 2021	$ 50,450	$ 526,135	$ 296,021	$ 1,749	$ 874,355
Net Income			25,921		25,921
Other Comprehensive Loss				(39)	(39)
TOTAL COMMON SHAREHOLDER'S EQUITY - MARCH 31, 2022	50,450	526,135	321,942	1,710	900,237
Net Income			13,167		13,167
Other Comprehensive Loss				(40)	(40)
TOTAL COMMON SHAREHOLDER'S EQUITY - JUNE 30, 2022	50,450	526,135	335,109	1,670	913,364
Net Income			11,595		11,595
Other Comprehensive Loss				(1,670)	(1,670)
TOTAL COMMON SHAREHOLDER'S EQUITY - SEPTEMBER 30, 2022	$ 50,450	$ 526,135	$ 346,704	$ —	$ 923,289
TOTAL COMMON SHAREHOLDER'S EQUITY - DECEMBER 31, 2022	$ 50,450	$ 526,287	$ 343,573	$ —	$ 920,310
Net Income			4,652		4,652
TOTAL COMMON SHAREHOLDER'S EQUITY - MARCH 31, 2023	50,450	526,287	348,225	—	924,962
Return of Capital to Parent		(52)			(52)
Net Income			1,873		1,873
TOTAL COMMON SHAREHOLDER'S EQUITY - JUNE 30, 2023	50,450	526,235	350,098	—	926,783
Capital Contribution from Parent		66			66
Net Income			14,120		14,120
TOTAL COMMON SHAREHOLDER'S EQUITY - SEPTEMBER 30, 2023	$ 50,450	$ 526,301	$ 364,218	$ —	$ 940,969

See Condensed Notes to Condensed Financial Statements beginning on page 9.

KENTUCKY POWER COMPANY
CONDENSED BALANCE SHEETS
ASSETS
September 30, 2023 and December 31, 2022
(in thousands)
(Unaudited)

	September 30, 2023	December 31, 2022
CURRENT ASSETS		
Cash and Cash Equivalents	$ 1,277	$ 2,684
Accounts Receivable:		
Customers	11,557	63,432
Affiliated Companies	13,299	10,818
Accrued Unbilled Revenues	4,219	35,002
Miscellaneous	88	72
Allowance for Uncollectible Accounts	(1)	(1,013)
Total Accounts Receivable	29,162	108,311
Fuel	69,349	21,994
Materials and Supplies	25,234	26,182
Risk Management Assets	6,932	8,463
Regulatory Asset for Under-Recovered Fuel Costs	6,291	23,241
Margin Deposits	710	960
Prepayments and Other Current Assets	5,332	2,512
TOTAL CURRENT ASSETS	144,287	194,347
PROPERTY, PLANT AND EQUIPMENT		
Electric:		
Generation	1,240,900	1,236,474
Transmission	819,866	801,838
Distribution	1,097,737	1,061,601
Other Property, Plant and Equipment	172,819	167,981
Construction Work in Progress	167,292	137,964
Total Property, Plant and Equipment	3,498,614	3,405,858
Accumulated Depreciation and Amortization	1,192,804	1,156,221
TOTAL PROPERTY, PLANT AND EQUIPMENT – NET	2,305,810	2,249,637
OTHER NONCURRENT ASSETS		
Regulatory Assets	526,311	504,185
Deferred Charges and Other Noncurrent Assets	42,999	58,936
TOTAL OTHER NONCURRENT ASSETS	569,310	563,121
TOTAL ASSETS	$ 3,019,407	$ 3,007,105

See Condensed Notes to Condensed Financial Statements beginning on page 9.

KENTUCKY POWER COMPANY
CONDENSED BALANCE SHEETS
LIABILITIES AND COMMON SHAREHOLDER'S EQUITY
September 30, 2023 and December 31, 2022
(Unaudited)

	September 30, 2023	December 31, 2022
	(in thousands)	
CURRENT LIABILITIES		
Advances from Affiliates	$ 100,886	$ 94,428
Accounts Payable:		
General	41,222	56,969
Affiliated Companies	44,900	51,076
Long-term Debt Due Within One Year – Nonaffiliated	490,000	490,000
Customer Deposits	40,887	38,784
Accrued Taxes	22,834	40,272
Obligations Under Operating Leases	140	128
Other Current Liabilities	32,849	25,827
TOTAL CURRENT LIABILITIES	773,718	797,484
NONCURRENT LIABILITIES		
Long-term Debt – Nonaffiliated	688,315	688,448
Long-term Debt – Affiliated	25,000	—
Deferred Income Taxes	465,220	456,217
Regulatory Liabilities and Deferred Investment Tax Credits	94,916	108,853
Asset Retirement Obligations	18,420	18,447
Employee Benefits and Pension Obligations	7,961	9,736
Obligations Under Operating Leases	561	450
Deferred Credits and Other Noncurrent Liabilities	4,327	7,160
TOTAL NONCURRENT LIABILITIES	1,304,720	1,289,311
TOTAL LIABILITIES	2,078,438	2,086,795
Rate Matters (Note 4)		
Commitments and Contingencies (Note 5)		
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	526,301	526,287
Retained Earnings	364,218	343,573
TOTAL COMMON SHAREHOLDER'S EQUITY	940,969	920,310
TOTAL LIABILITIES AND COMMON SHAREHOLDER'S EQUITY	$ 3,019,407	$ 3,007,105

See Condensed Notes to Condensed Financial Statements beginning on page 9.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF CASH FLOWS
For the Nine Months Ended September 30, 2023 and 2022
(in thousands)
(Unaudited)

	Nine Months Ended September 30, 2023	2022
OPERATING ACTIVITIES		
Net Income	$ 20,645	$ 50,683
Adjustments to Reconcile Net Income to Net Cash Flows from Operating Activities:		
Depreciation and Amortization	93,501	92,116
Deferred Income Taxes	(23,071)	(12,650)
Allowance for Equity Funds Used During Construction	(586)	(646)
Mark-to-Market of Risk Management Contracts	4,903	(8,425)
Pension and Postemployment Benefit Reserves	(3,090)	32,042
Property Taxes	16,998	14,654
Deferred Fuel Over/Under-Recovery, Net	16,950	(16,209)
Change in Regulatory Assets	(21,474)	(28,525)
Change in Other Noncurrent Assets	(6,712)	1,827
Change in Other Noncurrent Liabilities	(11,291)	9,190
Changes in Certain Components of Working Capital:		
Accounts Receivable, Net	79,196	(47,805)
Fuel, Materials and Supplies	(46,434)	(6,031)
Margin Deposits	250	14,106
Accounts Payable	(20,680)	3,143
Accrued Taxes, Net	(18,740)	(22,537)
Other Current Assets	(1,502)	40
Other Current Liabilities	5,897	(3,530)
Net Cash Flows from Operating Activities	84,760	71,443
INVESTING ACTIVITIES		
Construction Expenditures	(117,797)	(149,041)
Proceeds from Sales of Assets	76	7,995
Other Investing Activities	657	417
Net Cash Flows Used for Investing Activities	(117,064)	(140,629)
FINANCING ACTIVITIES		
Capital Contribution from Parent	66	—
Return of Capital to Parent	(52)	—
Issuance of Long-term Debt – Nonaffiliated	64,485	149,873
Issuance of Long-term Debt – Affiliated	25,000	—
Change in Advances from Affiliates, Net	6,458	599
Retirement of Long-term Debt – Nonaffiliated	(65,000)	(75,000)
Principal Payments for Finance Lease Obligations	(61)	(2,705)
Other Financing Activities	1	6
Net Cash Flows from Financing Activities	30,897	72,773
Net Increase (Decrease) in Cash and Cash Equivalents	(1,407)	3,587
Cash and Cash Equivalents at Beginning of Period	2,684	763
Cash and Cash Equivalents at End of Period	$ 1,277	$ 4,350
SUPPLEMENTARY INFORMATION		
Cash Paid for Interest, Net of Capitalized Amounts	$ 44,191	$ 28,635
Net Cash Paid (Received) for Income Taxes	631	(2,234)
Noncash Acquisitions Under Finance Leases	371	126
Construction Expenditures Included in Current Liabilities as of September 30,	19,327	31,514

See Condensed Notes to Condensed Financial Statements beginning on page 9.

INDEX OF 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 statement of the net income, financial position and cash flows for the interim periods. Net income for the three and nine months ended September 30, 2023 is not necessarily indicative of results that may be expected for the year ending December 31, 2023. The condensed financial statements are unaudited and should be read in conjunction with the audited 2022 financial statements and notes thereto, which are included in KPCo's 2022 Annual Report.

Termination of Planned Disposition of KPCo and KTCo

In October 2021, AEP entered into a Stock Purchase Agreement (SPA) to sell KPCo and KTCo to Liberty Utilities Co., a subsidiary of Algonquin Power & Utilities Corp. (Liberty), for approximately a $2.85 billion enterprise value. The SPA was subsequently amended in September 2022 to reduce the purchase price to approximately $2.646 billion. The sale required approval from the KPSC and from the FERC under Section 203 of the Federal Power Act. The SPA contained certain termination rights if the closing of the sale did not occur by April 26, 2023.

In May 2022, the KPSC approved the sale of KPCo to Liberty subject to certain conditions contingent upon the closing of the sale. In December 2022, the FERC issued an order denying, without prejudice, authorization of the proposed sale stating the applicants failed to demonstrate the proposed transaction will not have an adverse effect on rates. In February 2023, a new filing for approval under Section 203 of the Federal Power Act was submitted. In March 2023, the KPSC and other intervenors made filings recommending the FERC reject AEP and Liberty's new Section 203 application seeking approval of the sale.

In April 2023, AEP, AEPTCo and Liberty entered into a Mutual Termination Agreement (Termination Agreement) terminating the SPA. The parties entered into the Termination Agreement as all of the conditions precedent to closing the sale could not be satisfied prior to April 26, 2023.

Subsequent Events

Management reviewed subsequent events through November 2, 2023, the date that the third quarter 2023 report was available to be issued.

2. NEW ACCOUNTING STANDARDS

During the FASB's standard-setting process and upon issuance of final standards, management reviews the new accounting literature to determine its relevance, if any, to KPCo's business. There are no new standards expected to have a material impact on KPCo's financial statements.

3. COMPREHENSIVE INCOME

In September 2022, WPCo replaced KPCo as the operator of the Mitchell Plant. The employees and retirees of the plant were transferred to WPCo. KPCo had a $0 balance in AOCI as of September 30, 2023 and December 31, 2022. KPCo's balance in AOCI was $0 as of September 30, 2022 and the activity within AOCI was not material for the three and nine months ended September 30, 2022.

4. RATE MATTERS

As discussed in KPCo's 2022 Annual Report, KPCo is involved in rate and regulatory proceedings at the FERC and the KPSC. The Rate Matters note within KPCo's 2022 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 2023 and updates KPCo's 2022 Annual Report.

Regulatory Assets Pending Final Regulatory Approval

Noncurrent Regulatory Assets	September 30, 2023	December 31, 2022
	(in thousands)	
Regulatory Assets Currently Not Earning a Return		
Storm-Related Costs (a)	$ 78,728	$ 74,430
Other Regulatory Assets Pending Final Regulatory Approval	2,351	1,699
Total Regulatory Assets Pending Final Regulatory Approval	$ 81,079	$ 76,129

(a) KPCo has requested recovery of its deferred storm costs, related to 2020, 2021, 2022 and 2023 major storms, through securitization in its 2023 base rate and securitization case.

If these costs are ultimately determined not to be recoverable, it could reduce future net income and cash flows and impact financial condition.

Deferred Purchased Power Expenses

In September 2022, the KPSC initiated a proceeding to investigate the appropriate amortization period and recovery mechanism for the deferral of Kentucky Deferred Purchased Power Expenses related to the Rockport Plant Unit Power Agreement (UPA), as well as KPCo's ability to use the level of non-fuel, non-environmental Rockport UPA expense included in base rates to earn its authorized ROE in 2023 since the KPCo UPA ended in December 2022. KPCo requested the KPSC approve the terms related to each of the foregoing items as reflected in the settlement agreement in the 2017 Kentucky Base Rate Case, including recovery of the Kentucky Deferred Purchased Power Expenses over five years through a rider beginning in December 2022. In December 2022, the KPSC approved KPCo's request and recovery began through a rider, including recovery of an estimated allowed cost (Rockport Offset) of $22.8 million in accordance with the terms of the settlement agreement in the 2017 Kentucky Base Rate Case permitting KPCo to use the level of non-fuel, non-environmental Rockport UPA expense included in base rates to earn its authorized ROE in 2023. This estimated Rockport Offset is subject to true-up based on KPCo's actual 2023 financial results and KPSC review in the first quarter of 2024. The actual Rockport Offset cannot exceed $40.8 million. If the actual Rockport Offset is not recoverable, it could reduce future net income and cash flows and impact financial condition.

Fuel Adjustment Clause (FAC) Purchased Power Limitation

In May 2023, KPCo filed an application seeking authority to defer, for future recovery, approximately $11.5 million of December 2022 purchased power costs not recoverable through its FAC. This requested deferral accounting authority would have enabled KPCo to pursue securitization of these costs. In June 2023, the KPSC denied KPCo's request for deferral accounting authority. In July 2023, KPCo appealed this decision to the Kentucky state appellate court.

Also in June 2023, following its order denying KPCo's request for deferral accounting authority, the KPSC issued an order directing KPCo to show cause why it should not be subject to Kentucky statutory remedies, including fines and penalties, for failure to provide adequate service in its service territory. The KPSC's show cause order did not make any determination regarding the adequacy of KPCo's service. In July 2023, KPCo filed a response to the show cause order demonstrating that it has provided adequate service. A hearing is scheduled for the first quarter of 2024.

KPCo is requesting a prudency determination and recovery mechanism for these costs in its 2023 base rate. Unless and until KPCo is granted a recovery mechanism for these purchased power costs from the KPSC it will impact cash flows and financial condition. Additionally, if any fines or penalties are levied against KPCo relating to the show cause order, it will reduce net income and cash flows and impact financial condition.

2023 Kentucky Base Rate and Securitization Case

In June 2023, KPCo filed a request with the KPSC for a $93.9 million net annual increase in base rates based upon a proposed 9.9% ROE with the increase to be implemented no earlier than January 2024. The filing proposes no changes in depreciation rates and an annual level of storm restoration expense in base rates of approximately $1 million. KPCo also proposed to discontinue tracking of PJM transmission costs through a rider, and to instead collect an annual level of costs through base rates. In addition, KPCo has proposed a rider to recover certain distribution reliability investments and related incremental operation and maintenance expenses. KPCo also requested a prudency determination and recovery mechanism for approximately $15.5 million of purchased power costs not recoverable through its FAC since its last base case.

In conjunction with its June 2023 filing, KPCo further requested to finance, through the issuance of securitization bonds, approximately $471.2 million of regulatory assets recorded as of June 2023, including: (a) $289.2 million of plant retirement costs, (b) $79.3 million of deferred storm costs related to 2020, 2021, 2022 and 2023 major storms, (c) $52.2 million of deferred purchased power expenses and (d) $50.5 million of under-recovered purchased power rider costs. Plant retirement costs and deferred purchased power expenses have been deemed prudent in prior KPSC decisions. KPCo has requested a prudency determination in this proceeding for the deferred storm costs and under-recovered purchase power rider costs since the last base case. Consistent with Kentucky statutory requirements, the present value of the return on accumulated deferred income tax benefits related to plant retirement costs and deferred purchase power expenses were proposed to reduce the amount authorized to be financed through securitization.

In October 2023, various intervenors filed testimony recommending an annual base rate increase of $62.5 million based on ROEs ranging from 9.3% to 9.7%. Intervenors supported KPCo's securitization request, but proposed to include certain tax benefits as a reduction to the base rate revenue requirement. Intervenors also supported KPCo's proposal to discontinue tracking of PJM transmission costs through a rider, and to instead collect an annual level of costs through base rates. Other differences between KPCo's requested annual base rate increase and the intervenors' recommendations are primarily due to: (a) proposals to remove certain employee-related expenses from the revenue requirement, (b) opposition to various matters related to accumulated deferred income taxes, including opposition to KPCo's inclusion of its deferred tax asset associated with net operating loss on a stand-alone tax basis in rate base and a recommendation that KPCo not be permitted to recover a tax-related regulatory asset of approximately $33.4 million, (c) opposition to recovery of approximately $15.5 million of purchased power costs not recoverable through its FAC since its last base case, and (d) a recommendation that KPCo not earn a return on $41.7 million of prepaid pension and OPEB assets. In addition, intervenors expressed opposition to KPCo's proposed rider to recover certain distribution reliability investments and related incremental operation and maintenance expenses. KPCo is scheduled to file rebuttal testimony in November 2023. If any of these costs are not recoverable, it could reduce future net income and cash flows and impact financial condition.

5. 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 against KPCo 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 KPCo's 2022 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.

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. As of September 30, 2023, there were no material liabilities recorded for any indemnifications.

AEPSC conducts power purchase and sale activity on behalf of APCo, I&M, KPCo and WPCo, who are jointly and severally liable for activity conducted on their behalf.

Master Lease Agreements

KPCo 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, KPCo 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 September 30, 2023, the maximum potential loss for these lease agreements was $23 thousand assuming the fair value of the equipment is zero at the end of the lease term.

6. BENEFIT PLANS

KPCo participates in an AEP sponsored qualified pension plan and two unfunded nonqualified pension plans. Substantially all of KPCo's employees are covered by the qualified plan or both the qualified and nonqualified pension plans. KPCo also participates in OPEB plans sponsored by AEP to provide health and life insurance benefits for retired employees.

Components of Net Periodic Benefit Cost (Credit)

The following tables provide the components of KPCo's net periodic benefit cost (credit) for the plans:

	Pension Plans		OPEB	
	Three Months Ended September 30,		Three Months Ended September 30,	
	2023	2022	2023	2022
	(in thousands)			
Service Cost	$ 368	$ 791	$ 16	$ 52
Interest Cost	1,204	1,289	317	260
Expected Return on Plan Assets	(1,783)	(2,401)	(801)	(1,060)
Amortization of Prior Service Credit	—	—	(464)	(629)
Amortization of Net Actuarial Loss	—	536	112	—
Net Periodic Benefit Cost (Credit)	$ (211)	$ 215	$ (820)	$ (1,377)

	Pension Plans		OPEB	
	Nine Months Ended September 30,		Nine Months Ended September 30,	
	2023	2022	2023	2022
	(in thousands)			
Service Cost	$ 1,105	$ 2,373	$ 47	$ 157
Interest Cost	3,611	3,865	952	781
Expected Return on Plan Assets	(5,348)	(7,202)	(2,401)	(3,180)
Amortization of Prior Service Credit	—	—	(1,393)	(1,889)
Amortization of Net Actuarial Loss	—	1,608	334	—
Net Periodic Benefit Cost (Credit)	$ (632)	$ 644	$ (2,461)	$ (4,131)

7. DERIVATIVES AND HEDGING

OBJECTIVES FOR UTILIZATION OF DERIVATIVE INSTRUMENTS

AEPSC is agent for and transacts on behalf of KPCo.

KPCo is exposed to certain market risks as a major power producer and participant in the electricity, natural gas, coal and emission allowance markets. 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. Management utilizes derivative instruments to manage these risks.

STRATEGIES FOR UTILIZATION OF DERIVATIVE INSTRUMENTS TO ACHIEVE OBJECTIVES

Risk Management Strategies

The strategy surrounding the use of derivative instruments primarily focuses on managing risk exposures, future cash flows and creating value utilizing both economic and formal hedging strategies. The risk management strategies also include the use of derivative instruments for trading purposes which focus on seizing market opportunities to create value driven by expected changes in the market prices of the commodities. To accomplish these objectives, KPCo primarily employs risk management contracts including physical and financial forward purchase-and-sale contracts and, to a lesser extent, OTC swaps and options. 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.

KPCo utilizes power, capacity, coal, natural gas, interest rate and, to a lesser extent, heating oil, gasoline and other commodity contracts to manage the risk associated with the energy business. KPCo utilizes interest rate derivative contracts in order to manage the interest rate exposure associated with its commodity portfolio. For disclosure purposes, such risks are grouped as "Commodity," as these risks are related to energy risk management activities. KPCo may also utilize derivative contracts to manage interest rate risk associated with debt financing. For disclosure purposes, these risks are grouped as "Interest Rate." 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 the Board of Directors.

The following table represents the gross notional volume of KPCo's outstanding derivative contracts:

Primary Risk Exposure	September 30, 2023	December 31, 2022	Unit of Measure
	(in thousands)		
Commodity:			
Power	6,078	3,450	MWhs
Natural Gas	11,410	—	MMBtus

Cash Flow Hedging Strategies

KPCo utilizes cash flow hedges on certain derivative transactions for the purchase and sale of power ("Commodity") in order to manage the variable price risk related to forecasted purchases and sales. 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 purchases. KPCo does not hedge all commodity price risk.

KPCo may utilize a variety of interest rate derivative transactions in order to manage interest rate risk exposure. KPCo may also utilize interest rate derivative contracts to manage interest rate exposure related to future borrowings of fixed-rate debt. 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 on the balance sheets 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 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 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. The amount of cash collateral received from third-parties netted against short-term and long-term risk management assets and the amount of cash collateral paid to third-parties netted against short-term and long-term risk management liabilities were not material for KPCo as of September 30, 2023 and December 31, 2022.

The following tables represent the gross fair value of KPCo's derivative activity on the balance sheets. Unless shown as a separate line on the balance sheets due to materiality, Current Risk Management Assets are included in Prepayments and Other Current Assets, Long-term Risk Management Assets are included in Deferred Charges and Other Noncurrent Assets, Current Risk Management Liabilities are included in Other Current Liabilities and Long-term Risk Management Liabilities are included in Deferred Credits and Other Noncurrent Liabilities on the balance sheets.

	September 30, 2023		
Balance Sheet Location	**Risk Management Contracts – Commodity (a)**	**Gross Amounts Offset in the Statement of Financial Position (b)**	**Net Amounts of Assets/Liabilities Presented in the Statement of Financial Position (c)**
		(in thousands)	
Current Risk Management Assets	$ 9,233	$ (2,301)	$ 6,932
Long-term Risk Management Assets	197	(197)	—
Total Assets	9,430	(2,498)	6,932
Current Risk Management Liabilities	3,921	(2,301)	1,620
Long-term Risk Management Liabilities	707	(197)	510
Total Liabilities	4,628	(2,498)	2,130
Total MTM Derivative Contract Net Assets	$ 4,802	$ —	$ 4,802

	December 31, 2022		
Balance Sheet Location	**Risk Management Contracts – Commodity (a)**	**Gross Amounts Offset in the Statement of Financial Position (b)**	**Net Amounts of Assets/Liabilities Presented in the Statement of Financial Position (c)**
		(in thousands)	
Current Risk Management Assets	$ 8,607	$ (144)	$ 8,463
Long-term Risk Management Assets	137	(137)	—
Total Assets	8,744	(281)	8,463
Current Risk Management Liabilities	144	(144)	—
Long-term Risk Management Liabilities	137	(137)	—
Total Liabilities	281	(281)	—
Total MTM Derivative Contract Net Assets	$ 8,463	$ —	$ 8,463

(a) Derivative instruments within this category are disclosed as gross. These instruments are subject to master netting agreements and are presented on the balance sheets on a net basis in accordance with the accounting guidance for "Derivatives and Hedging."
(b) Amounts include counterparty netting of risk management and hedging contracts and associated cash collateral in accordance with the accounting guidance for "Derivatives and Hedging."
(c) All derivative contracts subject to a master netting arrangement or similar agreement are offset in the statement of financial position.

The table below presents KPCo's activity of derivative risk management contracts:

Amount of Gain (Loss) Recognized on Risk Management Contracts

	Three Months Ended September 30,		Nine Months Ended September 30,	
Location of Gain (Loss)	**2023**	**2022**	**2023**	**2022**
		(in thousands)		
Electric Generation, Transmission and Distribution Revenues	$ 1	$ 3	$ 1	$ 7
Purchased Electricity, Fuel and Other Consumables Used for Electric Generation	4	34	63	144
Other Operation	—	36	—	107
Maintenance	—	102	—	198
Regulatory Assets (a)	472	1	(682)	(25)
Regulatory Liabilities (a)	761	5,813	842	14,308
Total Gain on Risk Management Contracts	$ 1,238	$ 5,989	$ 224	$ 14,739

(a) Represents realized and unrealized gains and losses subject to regulatory accounting treatment recorded as either current or noncurrent on the balance sheets.

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 on the statements of income on an accrual basis.

The 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. Unrealized and realized gains and losses on derivative instruments held for trading purposes are included in revenues on a net basis on KPCo's statements of income. Unrealized and realized gains and losses on derivative instruments not held for trading purposes are included in revenues or expenses on KPCo's statements of income depending on the relevant facts and circumstances. Certain derivatives that economically hedge future commodity risk are recorded in the same line item on the statements of income as that of the associated risk being hedged. However, unrealized and some 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 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 gain or loss on the derivative instrument as a component of Accumulated Other Comprehensive Income (Loss) on the balance sheets until the period the hedged item affects Net Income.

Realized gains and losses on derivative contracts for the purchase and sale of power designated as cash flow hedges are included in Total Revenues or Purchased Electricity, Fuel and Other Consumables Used for Electric Generation on KPCo's statements of income, or in Regulatory Assets or Regulatory Liabilities on KPCo's balance sheets, depending on the specific nature of the risk being hedged. During the three and nine months ended September 30, 2023 and 2022, KPCo did not apply cash flow hedging to outstanding power derivatives.

KPCo reclassifies gains and losses on interest rate derivative hedges related to debt financings from Accumulated Other Comprehensive Income (Loss) on its balance sheets into Interest Expense on its statements of income in those periods in which hedged interest payments occur. During the three and nine months ended September 30, 2023 and 2022, KPCo did not apply cash flow hedging to outstanding interest rate derivatives.

There was no impact of cash flow hedges included in Accumulated Other Comprehensive Income (Loss) on KPCo's balance sheets as of September 30, 2023 and December 31, 2022.

The actual amounts that KPCo reclassifies from Accumulated Other Comprehensive Income (Loss) to Net Income can differ due to market price changes. As of September 30, 2023, KPCo is not hedging (with contracts subject to the accounting guidance for "Derivatives and Hedging") its exposure to variability in future cash flows related to forecasted transactions.

Credit Risk

Management mitigates 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. Management uses credit agency ratings and current market-based qualitative and quantitative data as well as financial statements to assess the financial health of counterparties on an ongoing basis.

Master agreements are typically used to facilitate the netting of cash flows associated with a single counterparty and may include collateral requirements. Collateral requirements in the form of cash, letters of credit, surety bonds and parental/affiliate guarantees may be obtained as security from counterparties in order to mitigate credit risk. Some master agreements include margining, which requires a counterparty to post cash or letters of credit in the event 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, master agreements allow for termination and liquidation of all positions in the event of a default including failure or inability to post collateral when required.

Collateral Triggering Events

Credit Downgrade Triggers

A limited number of derivative contracts include collateral triggering events, which include a requirement to maintain certain credit ratings. On an ongoing basis, AEP's risk management organization assesses the appropriateness of these collateral triggering events in contracts. KPCo has not experienced a downgrade below a specified credit rating threshold that would require the posting of additional collateral. As of September 30, 2023 and December 31, 2022, KPCo did not have derivative contracts with collateral triggering events in a net liability position.

Cross-Acceleration Triggers

Certain interest rate derivative contracts contain cross-acceleration provisions that, if triggered, would permit the counterparty to declare a default and require settlement of the outstanding payable. These cross-acceleration provisions could be triggered if there was a non-performance event by KPCo under any of their outstanding debt of at least $50 million and the lender on that debt has accelerated the entire repayment obligation. On an ongoing basis, AEP's risk management organization assesses the appropriateness of these cross-acceleration provisions in contracts. KPCo had no derivative contracts with cross-acceleration provisions in a net liability position as of September 30, 2023 and December 31, 2022, respectively. There was no cash collateral posted as of September 30, 2023 and December 31, 2022. If a cross-acceleration provision would have been triggered, settlement at fair value would have been required. KPCo had no derivative contracts with cross-acceleration provisions outstanding as of September 30, 2023 and December 31, 2022.

Cross-Default Triggers

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 by Parent or the obligor under outstanding debt or a third-party obligation that is $50 million or greater. On an ongoing basis, AEP's risk management organization assesses the appropriateness of these cross-default provisions in the contracts. KPCo had derivative contracts subject to cross-default provisions in a net liability position of $2 million and $0 as of September 30, 2023 and December 31, 2022, respectively. There was no cash collateral posted as of September 30, 2023 and December 31, 2022. If a cross-default provision would have been triggered, settlement at fair value would have been required.

8. 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.

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 derivatives 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 nonbinding 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. 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. Illiquid transactions, complex structured transactions, FTRs and counterparty credit risk may require nonmarket-based inputs. Some of these inputs may be internally developed or extrapolated and utilized to estimate fair value. When such inputs have a significant impact on the measurement of fair value, the instrument is categorized as Level 3. The main driver of contracts being classified as Level 3 is the inability to substantiate energy price curves in the market. A portion of the Level 3 instruments have been economically hedged which limits potential earnings volatility.

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 KPCo's Long-term Debt are summarized in the following table:

	September 30, 2023		December 31, 2022	
	Book Value	Fair Value	Book Value	Fair Value
	(in thousands)			
Long-term Debt	$ 1,203,315	$ 1,148,173	$ 1,178,448	$ 1,148,769

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 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
September 30, 2023

	Level 1	Level 2	Level 3	Other	Total
			(in thousands)		
Assets:					
Risk Management Assets					
Risk Management Commodity Contracts (a) (b)	$ —	$ 3,322	$ 5,830	$ (2,220)	$ 6,932
Liabilities:					
Risk Management Liabilities					
Risk Management Commodity Contracts (a) (b)	$ —	$ 4,044	$ 306	$ (2,220)	$ 2,130

December 31, 2022

	Level 1	Level 2	Level 3	Other	Total
			(in thousands)		
Assets:					
Risk Management Assets					
Risk Management Commodity Contracts (a) (b)	$ —	$ 137	$ 8,607	$ (281)	$ 8,463
Liabilities:					
Risk Management Liabilities					
Risk Management Commodity Contracts (a) (b)	$ —	$ 137	$ 144	$ (281)	$ —

(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) Substantially comprised of power contracts.

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 September 30, 2023	Net Risk Management Assets (Liabilities)
	(in thousands)
Balance as of June 30, 2023	$ 5,570
Realized Gain (Loss) Included in Net Income (or Changes in Net Assets) (a) (b)	859
Settlements	(2,276)
Transfers out of Level 3 (c)	(24)
Changes in Fair Value Allocated to Regulated Jurisdictions (d)	1,395
Balance as of September 30, 2023	$ 5,524

Three Months Ended September 30, 2022	Net Risk Management Assets (Liabilities)
	(in thousands)
Balance as of June 30, 2022	$ 13,549
Realized Gain (Loss) Included in Net Income (or Changes in Net Assets) (a) (b)	1,120
Settlements	(5,307)
Changes in Fair Value Allocated to Regulated Jurisdictions (d)	4,966
Balance as of September 30, 2022	$ 14,328

Nine Months Ended September 30, 2023	Net Risk Management Assets (Liabilities)
	(in thousands)
Balance as of December 31, 2022	$ 8,463
Realized Gain (Loss) Included in Net Income (or Changes in Net Assets) (a) (b)	(5,276)
Settlements	(3,187)
Changes in Fair Value Allocated to Regulated Jurisdictions (d)	5,524
Balance as of September 30, 2023	$ 5,524

Nine Months Ended September 30, 2022	Net Risk Management Assets (Liabilities)
	(in thousands)
Balance as of December 31, 2021	$ 5,871
Realized Gain (Loss) Included in Net Income (or Changes in Net Assets) (a) (b)	2,801
Settlements	(8,672)
Changes in Fair Value Allocated to Regulated Jurisdictions (d)	14,328
Balance as of September 30, 2022	$ 14,328

(a) Included in revenues on KPCo's 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) Transfers are recognized based on their value at the beginning of the reporting period that the transfer occurred.
(d) Relates to the net gains (losses) of those contracts that are not reflected on KPCo's statements of income. These changes in fair value are recorded as regulatory liabilities for net gains and as regulatory assets for net losses.

The following tables quantify the significant unobservable inputs used in developing the fair value of Level 3 positions:

Significant Unobservable Inputs
September 30, 2023

	Fair Value		Valuation	Significant Unobservable	Input/Range		
	Assets	Liabilities	Technique	Input (a)	Low	High	Weighted Average (b)
	(in thousands)						
FTRs	$ 5,830	$ 306	Discounted Cash Flow	Forward Market Price	$ (0.06)	$ 9.08	$ 1.06

December 31, 2022

	Fair Value		Valuation	Significant Unobservable	Input/Range		
	Assets	Liabilities	Technique	Input (a)	Low	High	Weighted Average (b)
	(in thousands)						
FTRs	$ 8,607	$ 144	Discounted Cash Flow	Forward Market Price	$ (3.10)	$ 18.79	$ 2.48

(a) Represents market prices in dollars per MWh.
(b) The weighted average is the product of the forward market price of the underlying commodity and volume weighted by term.

The following table provides the measurement uncertainty of fair value measurements to increases (decreases) in significant unobservable inputs related to Energy Contracts and FTRs as of September 30, 2023 and December 31, 2022:

Uncertainty of Fair Value Measurements

Significant Unobservable Input	Position	Change in Input	Impact on Fair Value Measurement
Forward Market Price	Buy	Increase (Decrease)	Higher (Lower)
Forward Market Price	Sell	Increase (Decrease)	Lower (Higher)

9. INCOME TAXES

Effective Tax Rates (ETR)

KPCo accounts for income taxes in interim periods in accordance with the accounting guidance for "Income Taxes." In accordance with the guidance the use of an estimated annual effective tax rate should be utilized to determine income tax expense unless a reliable estimate of the annual effective tax rate cannot be made, in which case the actual effective tax rate for the year to date should be utilized. KPCo's interim ETR reflects the actual year-to-date effective tax rate for 2023 and the estimated annual ETR for 2022, adjusted for tax expense associated with certain discrete items.

KPCo includes the amortization of Excess ADIT not subject to normalization requirements in the estimated annual ETR when regulatory proceedings instruct KPCo to provide the benefits of Tax Reform to customers over multiple interim periods. Certain regulatory proceedings instruct KPCo to provide the benefits of Tax Reform to customers in a single period (e.g. by applying the Excess ADIT not subject to normalization requirements against an existing regulatory asset balance) and in these circumstances, KPCo recognizes the tax benefit discretely in the period recorded. The annual amount of Excess ADIT approved by KPCo's regulatory commissions may not impact the ETR ratably during each interim period due to the variability of pretax book income between interim periods and the application of an estimated annual ETR.

The ETR for KPCo is included in the following table:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2023	2022	2023	2022
U.S. Federal Statutory Rate	21.0 %	21.0 %	21.0 %	21.0 %
Increase (decrease) due to:				
State Income Tax, net of Federal Benefit	2.5 %	(8.8)%	19.5 %	(2.5)%
Tax Reform Excess ADIT Reversal	(92.8)%	(44.1)%	859.2 %	(77.0)%
Flow Through	(1.8)%	(1.6)%	28.6 %	(0.2)%
AFUDC Equity	(0.2)%	(1.6)%	4.5 %	(1.2)%
Discrete Tax Adjustments	(4.9)%	— %	(18.9)%	(2.8)%
Other	(1.0)%	(2.3)%	(16.8)%	— %
Effective Income Tax Rate	(77.2)%	(37.4)%	897.1 %	(62.7)%

Federal and State Income Tax Audit Status

The statute of limitations for the IRS to examine KPCo and other AEP subsidiaries' originally filed federal return has expired for tax years 2016 and earlier. KPCo and other AEP subsidiaries have agreed to extend the statute of limitations on the 2017-2019 tax returns to October 31, 2024, to allow time for the current IRS audit to be completed including a refund claim approval by the Congressional Joint Committee on Taxation. The statute of limitations for the 2020 return is set to naturally expire in October 2024 as well.

The current IRS audit and associated refund claim evolved from a net operating loss carryback to 2015 that originated in the 2017 return. KPCo and other AEP subsidiaries have received and agreed to immaterial IRS proposed adjustments on the 2017 tax return. The exam is nearly complete, and KPCo and other AEP subsidiaries are currently working with the IRS to submit the refund claim to the Congressional Joint Committee on Taxation for resolution and final approval.

KPCo and other AEP subsidiaries file 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. Generally, the statutes of limitations have expired for tax years prior to 2017. In addition, management is monitoring and continues to evaluate the potential impact of federal legislation and corresponding state conformity.

Federal Legislation

In August 2022, President Biden signed H.R. 5376 into law, commonly known as the Inflation Reduction Act of 2022 or IRA. Most notably this budget reconciliation legislation creates a 15% minimum tax on adjusted financial statement income (Corporate Alternative Minimum Tax or CAMT), extends and increases the value of PTCs and ITCs, adds a nuclear and clean hydrogen PTC, an energy storage ITC and allows the sale or transfer of tax credits to third parties for cash. As further significant guidance from Treasury and the IRS is expected on the tax provisions in the IRA, KPCo and other AEP subsidiaries will continue to monitor any issued guidance and evaluate the impact on future net income, cash flows and financial condition.

In December 2022, the IRS released Notice 2023-7, which provided initial CAMT guidance that KPCo and other AEP subsidiaries can begin to rely on in 2023. Notably, the interim guidance in Notice 2023-7 confirmed the CAMT depreciation adjustment includes tax depreciation that is capitalized to inventory under §263A and recovered as part of cost of goods sold, providing significant relief to KPCo and other AEP subsidiaries potential CAMT exposure. In September 2023, the IRS released Notice 2023-64, which clarifies and supplements items in Notice 2023-7 and stated that additional guidance in the form of proposed regulations is expected. KPCo and other AEP subsidiaries will continue to monitor and assess any additional guidance.

KPCo and other AEP subsidiaries expect to be applicable corporations for purposes of the CAMT beginning in 2023. CAMT cash taxes are expected to be partially offset by regulatory recovery, the utilization of tax credits and additionally the cash inflow generated by the sale of tax credits. The sale of tax credits are presented in the operating section of the statements of cash flows consistent with the presentation of cash taxes paid. KPCo and other AEP subsidiaries will present the loss on sale of tax credits through income tax expense.

10. FINANCING ACTIVITIES

Long-term Debt

Long-term debt issued and retired during the first nine months of 2023 are shown in the tables below:

	Type of Debt	Principal Amount (a)	Interest Rate	Due Date
Issuances:		**(in thousands)**	**(%)**	
	Pollution Control Bonds	$ 65,000	4.70	2026
	Senior Notes	25,000	5.29	2028
Total Issuances		$ 90,000		

(a) Amounts indicated on the statements of cash flows are net of issuance costs and premium or discount and will not tie to the issuance amounts.

	Type of Debt	Principal Amount Paid	Interest Rate	Due Date
Retirements:		**(in thousands)**	**(%)**	
	Pollution Control Bonds	$ 65,000	2.35	2023

Dividend Restrictions

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

All of the dividends declared by KPCo are subject to a Federal Power Act requirement that prohibits the payment of dividends out of capital accounts in certain circumstances; payment of dividends is generally allowed out of retained earnings.

KPCo has credit agreements that contain a covenant that limit its debt to capitalization ratio to 67.5%. As of September 30, 2023, KPCo did not exceed its debt to capitalization limit. The method for calculating outstanding debt and capitalization is contractually-defined in the credit agreements.

The Federal Power Act restriction does not limit the ability of KPCo to pay dividends out of retained earnings.

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 its agreement filed with the FERC. The amounts of outstanding borrowings from the Utility Money Pool as of September 30, 2023 and December 31, 2022 are included in Advances from Affiliates on KPCo's balance sheets. KPCo's Utility Money Pool activity and corresponding authorized borrowing limit for the nine months ended September 30, 2023 are described in the following table:

Maximum Borrowings from the Utility Money Pool	Average Borrowings from the Utility Money Pool	Borrowings from the Utility Money Pool as of September 30, 2023	Authorized Short-Term Borrowing Limit
	(in thousands)		
$ 169,398	$ 124,394	$ 100,886	$ 180,000

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

Nine Months Ended September 30,	Maximum Interest Rate for Funds Borrowed from the Utility Money Pool	Minimum Interest Rate for Funds Borrowed from the Utility Money Pool	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 Borrowed from the Utility Money Pool	Average Interest Rate for Funds Loaned to the Utility Money Pool
2023	5.81 %	4.66 %	— %	— %	5.49 %	— %
2022	3.39 %	0.10 %	2.15 %	2.14 %	1.45 %	2.15 %

Securitized Accounts Receivables – AEP Credit

Under an affiliated receivables sales arrangement, KPCo sells, without recourse, certain of its customer accounts receivable and accrued unbilled revenue balances to AEP Credit. In January 2022, due to the expected sale to Liberty, KPCo ceased selling accounts receivable to AEP Credit. As a result, in the first quarter of 2022, KPCo began recording an allowance for uncollectible accounts on its balance sheet for those receivables no longer sold to AEP Credit. In September 2023, KPCo resumed selling accounts receivable to AEP Credit, due to the termination of the sale to Liberty, and the balance in KPCo's allowance for uncollectible accounts was transferred to AEP Credit. KPCo is charged a fee for each sale that is based on AEP Credit's financing costs, administrative costs and uncollectible accounts experience from previous purchases of KPCo's customer accounts receivable. No allowance for uncollectible accounts is recognized within KPCo's financial statements for customer accounts receivable sold to AEP Credit, and any bad debt stemming from these receivables would be recognized by AEP Credit. The costs of customer accounts receivable sold are reported in Other Operation expense on KPCo's statements of income. KPCo manages and services its accounts receivables sold.

AEP Credit's receivables securitization agreement provides a commitment of $900 million from bank conduits to purchase receivables. The agreement was amended in August 2023 to increase the commitment from $750 million and expires in September 2025. As of September 30, 2023, KPCo was in compliance with all requirements under the agreement.

KPCo's amounts of accounts receivable and accrued unbilled revenues sold under the sale of receivables agreement were $35.5 million and $0 as of September 30, 2023 and December 31, 2022, respectively.

The fees paid by KPCo to AEP Credit for customer accounts receivable sold for the three months ended September 30, 2023 and 2022 were $568 thousand and $0, respectively and for the nine months ended September 30, 2023 and 2022 were $568 thousand and $63 thousand, respectively.

KPCo's proceeds on the sale of receivables to AEP Credit for the three months ended September 30, 2023 and 2022 were $74.3 million and $0, respectively, and for the nine months ended September 30, 2023 and 2022 were $74.3 million and $65.6 million, respectively.

11. REVENUE FROM CONTRACTS WITH CUSTOMERS

Disaggregated Revenues from Contracts with Customers

The table below represents KPCo's revenues from contracts with customers, net of respective provisions for refund, by type of revenue:

	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
	(in thousands)			
Retail Revenues:				
Residential Revenues	$ 62,943	$ 79,716	$ 185,836	$ 232,404
Commercial Revenues	40,585	51,351	118,863	141,930
Industrial Revenues	35,130	46,678	112,984	131,362
Other Retail Revenues	469	530	1,479	1,580
Total Retail Revenues	139,127	178,275	419,162	507,276
Wholesale Revenues:				
Generation Revenues	6,105	11,017	12,046	27,776
Transmission Revenues (a)	7,888	7,925	22,894	23,581
Total Wholesale Revenues	13,993	18,942	34,940	51,357
Other Revenues from Contracts with Customers (b)	2,547	2,703	8,406	8,945
Total Revenues from Contracts with Customers	155,667	199,920	462,508	567,578
Other Revenues:				
Alternative Revenue Programs (b) (c)	1,211	(2,759)	4,402	(3,458)
Other Revenues	1	3	1	7
Total Other Revenues	1,212	(2,756)	4,403	(3,451)
Total Revenues	$ 156,879	$ 197,164	$ 466,911	$ 564,127

(a) Amounts include affiliated and nonaffiliated revenues. The affiliated revenues were $3.9 million and $4.8 million for the three months ended September 30, 2023 and 2022, respectively, and $11.5 million and $14.3 million for the nine months ended September 30, 2023 and 2022, respectively.
(b) Amounts include affiliated and nonaffiliated revenues.
(c) Alternative revenue programs in certain jurisdictions include regulatory mechanisms that periodically adjust for over/under collection of related revenues.

Fixed Performance Obligations

The following table represents KPCo's remaining fixed performance obligations satisfied over time as of September 30, 2023. Fixed performance obligations primarily include electricity sales for fixed amounts of energy and stand ready services into PJM's RPM market. KPCo elected to apply the exemption to not disclose the value of unsatisfied performance obligations for contracts with an original expected term of one year or less. Due to the annual establishment of revenue requirements, transmission revenues are excluded from the table below. The amounts shown in the table below include affiliated and nonaffiliated revenues.

2023	2024-2025	2026-2027	After 2027	Total
		(in thousands)		
$ 359	$ 2,870	$ 2,870	$ 1,435	$ 7,534

Contract Assets and Liabilities

Contract assets are recognized when KPCo 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. KPCo did not have material contract assets as of September 30, 2023 and December 31, 2022, respectively.

When KPCo 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. KPCo's contract liabilities typically arise from advanced payments of services provided primarily with respect to joint use agreements for utility poles. KPCo did not have material contract liabilities as of September 30, 2023 and December 31, 2022, respectively.

Accounts Receivable from Contracts with Customers

Accounts receivable from contracts with customers are presented on KPCo's balance sheets within the Accounts Receivable - Customers line item. KPCo'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 were not material as of September 30, 2023 and December 31, 2022. See "Securitized Accounts Receivable - AEP Credit" section of Note 10 for additional information related to AEP Credit's securitized accounts receivable.

The amount of affiliated accounts receivable from contracts with customers included in Accounts Receivable - Affiliated Companies on KPCo's balance sheets were \$11.4 million and \$9.1 million, respectively, as of September 30, 2023 and December 31, 2022.