AEP Generating Company

2018 Annual Report

Audited Financial Statements

AMERICAN ELECTRIC POWER®

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 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.
AFUDC	Allowance for Funds Used During Construction.
AGR	AEP Generation Resources Inc., a competitive AEP subsidiary that acquired the generation assets and liabilities of OPCo.
ASU	Accounting Standards Update.
CCT	Cook Coal Terminal.
CWIP	Construction Work in Progress.
EIS	Energy Insurance Services, Inc., a nonaffiliated captive insurance company and consolidated variable interest entity of AEP.
FASB	Financial Accounting Standards Board.
Federal EPA	United States Environmental Protection Agency.
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.
IURC	Indiana Utility Regulatory Commission.
KPCo	Kentucky Power Company, an AEP electric utility subsidiary.
MW	Megawatt.
NO_x	Nitrogen oxide.
NSR	New Source Review.
OPCo	Ohio Power Company, an AEP electric utility subsidiary.
OPEB	Other Postretirement Benefits.
Parent	American Electric Power Company, Inc., the equity owner of AEP subsidiaries within the AEP consolidation.
PSO	Public Service Company of Oklahoma, an AEP electric utility subsidiary.
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.
SWEPCo	Southwestern Electric Power Company, an AEP electric utility subsidiary.
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.
UMWA	United Mine Workers of America.
UPA	Unit Power Agreement.
Utility Money Pool	Centralized funding mechanism AEP uses to meet the short-term cash requirements of certain utility subsidiaries.
VIE	Variable Interest Entity.

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Report of Independent Auditors

To the Board of Directors and Management of
AEP Generating Company

We have audited the accompanying financial statements of AEP Generating Company, which comprise the balance sheets as of December 31, 2018 and 2017, and the related statements of income, changes in common shareholder's equity, and cash flows for the years then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on the financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of AEP Generating Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

February 21, 2019

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AEP GENERATING COMPANY
STATEMENTS OF INCOME
For the Years Ended December 31, 2018 and 2017
(in thousands)

	Years Ended December 31, 2018	2017
REVENUES		
Sales to AEP Affiliates	$ 339,869	$ 340,871
Other Revenues – Affiliated	18,082	15,507
Other Revenues – Nonaffiliated	1,997	3,581
TOTAL REVENUES	359,948	359,959
EXPENSES		
Fuel and Other Consumables Used for Electric Generation	163,379	168,079
Rent – Rockport Plant, Unit 2	68,283	68,283
Other Operation	25,960	26,717
Maintenance	27,153	21,354
Gain on Sale of Lawrenceburg Plant	—	(355,588)
Depreciation and Amortization	46,364	42,082
Taxes Other Than Income Taxes	4,514	4,408
TOTAL (INCOME) EXPENSES	335,653	(24,665)
OPERATING INCOME	24,295	384,624
Other Income (Expense):		
Interest Income	2,683	2,572
Allowance for Equity Funds Used During Construction	844	3,060
Non-Service Cost Components of Net Periodic Benefit Cost	1,042	570
Interest Expense	(5,262)	(4,840)
INCOME BEFORE INCOME TAX EXPENSE (BENEFIT)	23,602	385,986
Income Tax Expense (Benefit)	(6,836)	114,528
NET INCOME	$ 30,438	$ 271,458

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

See Notes to Financial Statements beginning on page 8.

AEP GENERATING COMPANY
STATEMENTS OF CHANGES IN COMMON SHAREHOLDER'S EQUITY
For the Years Ended December 31, 2018 and 2017
(in thousands)

	Common Stock	Paid-in Capital	Retained Earnings	Total
TOTAL COMMON SHAREHOLDER'S EQUITY – DECEMBER 31, 2016	$ 1,000	$ 285,487	$ 23,017	$ 309,504
Capital Contribution Returned to Parent		(110,000)		(110,000)
Common Stock Dividends			(200,000)	(200,000)
Net Income			271,458	271,458
TOTAL COMMON SHAREHOLDER'S EQUITY – DECEMBER 31, 2017	1,000	175,487	94,475	270,962
Capital Contribution Returned to Parent		(10,000)		(10,000)
Common Stock Dividends			(70,000)	(70,000)
Net Income			30,438	30,438
TOTAL COMMON SHAREHOLDER'S EQUITY – DECEMBER 31, 2018	$ 1,000	$ 165,487	$ 54,913	$ 221,400

See Notes to Financial Statements beginning on page 8.

AEP GENERATING COMPANY
BALANCE SHEETS
ASSETS
December 31, 2018 and 2017
(in thousands)

	December 31, 2018	December 31, 2017
CURRENT ASSETS		
Advances to Affiliates	$ 70,904	$ 94,165
Accounts Receivable:		
Customers	466	31
Affiliated Companies	30,196	36,985
Miscellaneous	—	1,986
Total Accounts Receivable	30,662	39,002
Fuel	37,289	31,355
Materials and Supplies	18,062	19,456
Prepayments and Other Current Assets	2,128	3,379
TOTAL CURRENT ASSETS	159,045	187,357
PROPERTY, PLANT AND EQUIPMENT		
Electric Generation	1,125,208	1,111,563
Other Property, Plant and Equipment	35,564	35,316
Construction Work in Progress	50,525	27,721
Total Property, Plant and Equipment	1,211,297	1,174,600
Accumulated Depreciation and Amortization	719,684	677,587
TOTAL PROPERTY, PLANT AND EQUIPMENT – NET	491,613	497,013
OTHER NONCURRENT ASSETS		
Regulatory Assets	14,671	15,865
Deferred Charges and Other Noncurrent Assets	1,871	1,512
TOTAL OTHER NONCURRENT ASSETS	16,542	17,377
TOTAL ASSETS	$ 667,200	$ 701,747

See Notes to Financial Statements beginning on page 8.

AEP GENERATING COMPANY
BALANCE SHEETS
LIABILITIES AND COMMON SHAREHOLDER'S EQUITY
December 31, 2018 and 2017

	December 31,	
	2018	**2017**
CURRENT LIABILITIES	**(in thousands)**	
Accounts Payable:		
General	$ 2,151	$ 1,958
Affiliated Companies	23,250	19,988
Long-term Debt Due Within One Year – Nonaffiliated	45,000	169,891
Accrued Taxes	6,451	14,555
Accrued Rent – Rockport Plant, Unit 2	4,963	4,963
Other Current Liabilities	3,463	3,948
TOTAL CURRENT LIABILITIES	85,278	215,303
NONCURRENT LIABILITIES		
Long-term Debt – Nonaffiliated	149,988	—
Deferred Income Taxes	30,872	30,131
Regulatory Liabilities and Deferred Investment Tax Credits	90,008	84,673
Deferred Gain on Sale-and-Leaseback – Rockport Plant, Unit 2	21,911	27,482
Deferred Credits and Other Noncurrent Liabilities	67,743	73,196
TOTAL NONCURRENT LIABILITIES	360,522	215,482
TOTAL LIABILITIES	445,800	430,785
Commitments and Contingencies (Note 4)		
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	175,487
Retained Earnings	54,913	94,475
TOTAL COMMON SHAREHOLDER'S EQUITY	221,400	270,962
TOTAL LIABILITIES AND COMMON SHAREHOLDER'S EQUITY	$ 667,200	$ 701,747

See Notes to Financial Statements beginning on page 8.

AEP GENERATING COMPANY
STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2018 and 2017
(in thousands)

	Years Ended December 31, 2018	2017
OPERATING ACTIVITIES		
Net Income	$ 30,438	$ 271,458
Adjustments to Reconcile Net Income to Net Cash Flows from (Used for) Operating Activities:		
Depreciation and Amortization	46,364	42,082
Deferred Income Taxes	2,496	(18,890)
Deferred Investment Tax Credits	(1,970)	(1,969)
Amortization of Deferred Gain on Sale-and-Leaseback – Rockport Plant, Unit 2	(5,571)	(5,571)
Allowance for Equity Funds Used During Construction	(844)	(3,060)
Gain on Sale of Lawrenceburg Plant	—	(355,588)
Change in Other Noncurrent Assets	1,172	(563)
Change in Other Noncurrent Liabilities	(1,313)	136
Changes in Certain Components of Working Capital:		
Accounts Receivable	8,340	24,784
Fuel, Materials and Supplies	(4,540)	(522)
Accounts Payable	3,455	(25,336)
Accrued Taxes, Net	(7,013)	2,621
Other Current Assets	170	(7,205)
Other Current Liabilities	(103)	(2,600)
Net Cash Flows from (Used for) Operating Activities	71,081	(80,223)
INVESTING ACTIVITIES		
Construction Expenditures	(37,709)	(61,459)
Change in Advances to Affiliates, Net	23,261	(75,128)
Proceeds from Sale of Lawrenceburg Plant	—	726,300
Other Investing Activities	164	(7)
Net Cash Flows from (Used for) Investing Activities	(14,284)	589,706
FINANCING ACTIVITIES		
Capital Contribution Returned to Parent	(10,000)	(110,000)
Issuance of Long-term Debt – Nonaffiliated	149,988	—
Retirement of Long-term Debt – Nonaffiliated	(125,000)	(152,727)
Make Whole Premium on Extinguishment of Long-term Debt	—	(44,884)
Principal Payments for Capital Lease Obligations	(1,801)	(1,881)
Dividends Paid on Common Stock	(70,000)	(200,000)
Other Financing Activities	16	9
Net Cash Flows Used for Financing Activities	(56,797)	(509,483)
Net Change in Cash and Cash Equivalents	—	—
Cash and Cash Equivalents at Beginning of Period	—	—
Cash and Cash Equivalents at End of Period	$ —	$ —
SUPPLEMENTARY INFORMATION		
Cash Paid for Interest, Net of Capitalized Amounts	$ 4,155	$ 6,658
Net Cash Paid (Received) for Income Taxes	(166)	131,076
Noncash Acquisitions Under Capital Leases	195	288
Construction Expenditures Included in Current Liabilities as of December 31,	118	86

See Notes to Financial Statements beginning on page 8.

INDEX OF NOTES TO FINANCIAL STATEMENTS

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION

AEGCo engages in the generation and wholesale sale of electric power to its affiliates, AGR, I&M and KPCo. AEGCo and I&M co-own Unit 1 of the Rockport Plant. Unit 2 of the Rockport Plant is owned by a third party and leased to I&M and AEGCo. I&M operates the Rockport Plant. AEGCo derives operating revenues from the sale of Rockport Plant energy and capacity to I&M and KPCo pursuant to FERC-approved long-term UPAs through December 2022. Under the terms of its UPA, I&M agreed to purchase all of AEGCo's Rockport energy and capacity unless it is sold to other utilities or affiliates. I&M assigned 30% of its rights to AEGCo's energy and capacity to KPCo. AEGCo also owns CCT which performs coal transloading services for I&M and railcar maintenance services for I&M, PSO and SWEPCo.

In 2007, OPCo and AEGCo entered into a 10-year UPA for the entire output from the Lawrenceburg Plant. The UPA had an option for an additional 2-year period. Effective January 2014, OPCo assigned its rights and liabilities under the Lawrenceburg UPA to AGR, which included AGR's option to extend for an additional 2 years. I&M operated the plant under an agreement with AEGCo. Under the UPA, AGR paid AEGCo for the capacity, depreciation, fuel, operation and maintenance and tax expenses. These payments were due regardless of whether the plant was operating. The fuel and operation and maintenance payments were based on actual costs incurred. All expenses were trued up periodically. In September 2016, AEP signed a Purchase and Sale Agreement to sell the Lawrenceburg Plant to a nonaffiliated party. The sale closed in January 2017. The UPA terminated upon closing of the sale.

The UPAs provide for a FERC-approved rate of return on common equity, a return on other capital (net of temporary cash investments) and recovery of costs including operation and maintenance, fuel and taxes. Under the terms of the UPAs, AEGCo accumulates all expenses monthly and prepares bills for its affiliates. In the month the expenses are incurred, AEGCo recognizes the billing revenues and establishes a receivable from the affiliated companies. The costs of operating the plants are billed to the affiliates receiving the benefits under the UPAs.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Rates and Service Regulation

The FERC regulates AEGCo's rates and affiliated transactions, including AEPSC intercompany service billings which are generally at cost, under the 2005 Public Utility Holding Company Act and the Federal Power Act. The FERC also has jurisdiction over the issuances and acquisitions of securities of public utility subsidiaries, the acquisition or sale of certain utility assets and mergers with another electric utility or holding company. For non-power goods and services, the FERC requires a nonregulated affiliate to bill an affiliated public utility company at no more than market while a public utility must bill the higher of cost or market to a nonregulated affiliate. Both the FERC and state regulatory commissions are permitted to review and audit the relevant books and records of companies within a public utility holding company system.

The FERC regulates wholesale power markets and wholesale power transactions. AEGCo's wholesale power transactions are generally cost-based regulated under FERC-approved unit power agreements.

Accounting for the Effects of Cost-Based Regulation

As a rate-regulated electric public utility company, AEGCo's financial statements reflect the actions of regulators that result in the recognition of certain revenues and expenses in different time periods than enterprises that are not rate-regulated. In accordance with accounting guidance for "Regulated Operations," AEGCo records regulatory assets (deferred expenses) and regulatory liabilities (deferred revenue reductions or refunds) to reflect the economic effects of regulation in the same accounting period by matching expenses with their recovery through regulated revenues and by matching income with its passage to customers in cost-based regulated rates.

Use of Estimates

The preparation of these financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. These estimates include, but are not limited to, inventory valuation, long-lived asset impairment, the effects of regulation, long-lived asset recovery and the effects of contingencies. The estimates and assumptions used are based upon management's evaluation of the relevant facts and circumstances as of the date of the financial statements. Actual results could ultimately differ from those estimates.

Inventory

Fossil fuel inventories and materials and supplies inventories are carried at average cost.

Property, Plant and Equipment

Electric utility property, plant and equipment are stated at original cost. Additions, major replacements and betterments are added to the plant accounts. Under the group composite method of depreciation, continuous interim routine replacements of items such as boiler tubes, pumps, motors, etc. result in original cost retirements, less salvage, being charged to accumulated depreciation. The group composite method of depreciation assumes that on average, asset components are retired at the end of their useful lives and thus there is no gain or loss. The equipment in each primary electric plant account is identified as a separate group. The depreciation rates that are established take into account the past history of interim capital replacements and the amount of removal cost incurred and salvage received. These rates and the related lives are subject to periodic review. Removal costs accrued are typically recorded as regulatory liabilities when the revenue received for removal costs accrued exceeds actual removal costs incurred. The asset removal costs liability is relieved as removal costs are incurred. A regulatory asset balance will occur if actual removal costs incurred exceed accumulated removal costs accrued.

The costs of labor, materials and overhead incurred to operate and maintain plant and equipment are included in operating expenses.

Long-lived assets are required to be tested for impairment when it is determined that the carrying value of the assets may no longer be recoverable or when the assets meet the held-for-sale criteria under the accounting guidance for "Impairment or Disposal of Long-Lived Assets." When it becomes probable that an asset in service or an asset under construction will be abandoned and regulatory cost recovery has been disallowed or is not probable, the cost of that asset shall be removed from plant-in-service or CWIP and charged to expense.

The fair value of an asset is the amount at which that asset could be bought or sold in a current transaction between willing parties, as opposed to a forced or liquidation sale. Quoted market prices in active markets are the best evidence of fair value and are used as the basis for the measurement, if available. In the absence of quoted prices for identical or similar assets in active markets, fair value is estimated using various internal and external valuation methods including cash flow analysis and appraisals.

Allowance for Funds Used During Construction

AFUDC represents the estimated cost of borrowed and equity funds used to finance construction projects that is capitalized and recovered through depreciation over the service life of regulated electric utility plant. AEGCo records the equity component of AFUDC in Allowance for Equity Funds Used During Construction and the debt component of AFUDC as a reduction to Interest Expense.

Valuation of Nonderivative Financial Instruments

The book values of Advances to Affiliate, Accounts Receivable and Accounts Payable approximate fair value because of the short-term maturity of these instruments.

Fair Value Measurements of Assets and Liabilities

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.

AEP utilizes its trustee's external pricing service to estimate the fair value of the underlying investments held in the benefit plan trusts. AEP's investment managers review and validate the prices utilized by the trustee to determine fair value. AEP's management performs its own valuation testing to verify the fair values of the securities. AEP receives audit reports of the trustee's operating controls and valuation processes. The trustee uses multiple pricing vendors for the assets held in the trusts.

Assets in the benefits trusts are classified using the following methods. Equities are classified as Level 1 holdings if they are actively traded on exchanges. Items classified as Level 1 are investments in money market funds, fixed income and equity mutual funds and equity securities. They are valued based on observable inputs primarily unadjusted quoted prices in active markets for identical assets. Items classified as Level 2 are primarily investments in individual fixed income securities. Fixed income securities generally do not trade on exchanges and do not have an official closing price but their valuation inputs are based on observable market data. Pricing vendors calculate bond valuations using financial models and matrices. The models use observable inputs including yields on benchmark securities, quotes by securities brokers, rating agency actions, discounts or premiums on securities compared to par prices, changes in yields for U.S. Treasury securities, corporate actions by bond issuers, prepayment schedules and histories, economic events and, for certain securities, adjustments to yields to reflect changes in the rate of inflation. Other securities with model-derived valuation inputs that are observable are also classified as Level 2 investments. Investments with unobservable valuation inputs are classified as Level 3 investments. Investments classified as Other are valued using Net Asset Value as a practical expedient. Items classified as Other are primarily cash equivalent funds, common collective trusts, commingled funds, structured products, private equity, real estate, infrastructure and alternative credit investments. These investments do not have a readily determinable fair value or they contain redemption restrictions which may include the right to suspend redemptions under certain circumstances. Redemption restrictions may also prevent certain investments from being redeemed at the reporting date for the underlying value.

Revenue Recognition and Accounts Receivable

Under terms of the UPAs, AEGCo accumulates all expenses monthly and prepares bills for its affiliates. In the month the expenses are incurred, AEGCo recognizes the billing revenues and establishes receivables from the affiliate companies.

AEGCo also accumulates costs for its CCT division and prepares bills monthly for both affiliated and nonaffiliated companies.

Maintenance

Maintenance costs are expensed as incurred.

Income Taxes and Investment Tax Credits

AEGCo uses the liability method of accounting for income taxes. Under the liability method, deferred income taxes are provided for all temporary differences between the book and tax basis of assets and liabilities which will result in a future tax consequence. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which the temporary differences are expected to be recovered or settled. AEGCo revalued deferred tax assets and liabilities at the new federal corporate income tax rate of 21% in December 2017. See Note 8 for additional information related to Tax Reform.

When the flow-through method of accounting for temporary differences is reflected in regulated revenues (that is, when deferred taxes are not included in the cost of service for determining regulated rates for electricity), deferred income taxes are recorded and related regulatory assets and liabilities are established to match the regulated revenues and tax expense.

AEGCo applies deferral methodology for the recognition of ITC. Deferred ITC is amortized to income tax expense over the life of the asset. Amortization of deferred ITC begins when the asset is placed into service, except where regulatory commissions reflect ITC in the rate-making process, then amortization begins when the cash tax benefit is recognized.

AEGCo accounts for uncertain tax positions in accordance with the accounting guidance for "Income Taxes." AEGCo classifies interest expense or income related to uncertain tax positions as interest expense or income as appropriate and classifies penalties as Other Operation expense.

Debt

Gains and losses from the reacquisition of debt used to finance AEGCo's plants are deferred and amortized over the remaining term of the reacquired debt in accordance with their rate-making treatment unless the debt is refinanced. If the reacquired debt is refinanced, the reacquisition costs are generally deferred and amortized over the term of the replacement debt consistent with its recovery in rates.

Debt discount or premium and debt issuance expenses are deferred and amortized generally utilizing the straight-line method over the term of the related debt. The straight-line method approximates the effective interest method and is consistent with the treatment in rates for regulated operations. The net amortization expense is included in Interest Expense on the statements of income.

Pension and OPEB Plans

AEGCo participates in an AEP sponsored qualified pension plan. Substantially all of AEGCo's employees other than certain longer service UMWA members are covered by the qualified plan. UMWA pension benefits are provided through the United Mine Workers of America 1974 Pension Plan, a multiemployer plan, to CCT employees who are not covered by the qualified plan. AEGCo also participates in OPEB plans sponsored by AEP to provide health and life insurance benefits for retired employees as well as certain unionized employees, retirees and their survivors who meet eligibility requirements. AEGCo accounts for its participation in the AEP sponsored pension and OPEB plans using multiple-employer accounting. See Note 6 - Benefit Plans for additional information including significant accounting policies associated with the plans.

Investments Held in Trust for Future Liabilities

AEP has several trust funds with significant investments intended to provide for future payments of pension and OPEB benefits. All of the trust funds' investments are diversified and managed in compliance with all laws and regulations. The investment strategy for the trust funds is to use a diversified portfolio of investments to achieve an acceptable rate of return while managing the investment risk of the assets relative to the associated liabilities. To minimize investment risk, the trust funds are broadly diversified among classes of assets, investment strategies and investment managers. Management regularly reviews the actual asset allocations and periodically rebalances the investments to targeted allocations when appropriate. Investment policies and guidelines allow investment managers in approved strategies to use financial derivatives to obtain or manage market exposures and to hedge assets and liabilities. The investments are reported at fair value under the "Fair Value Measurements and Disclosures" accounting guidance.

Benefit Plans

All benefit plan assets are invested in accordance with each plan's investment policy. The investment policy outlines the investment objectives, strategies and target asset allocations by plan.

The investment philosophies for AEP's benefit plans support the allocation of assets to minimize risks and optimize net returns. Strategies used include:

- Maintaining a long-term investment horizon.
- Diversifying assets to help control volatility of returns at acceptable levels.
- Managing fees, transaction costs and tax liabilities to maximize investment earnings.
- Using active management of investments where appropriate risk/return opportunities exist.
- Keeping portfolio structure style-neutral to limit volatility compared to applicable benchmarks.
- Using alternative asset classes such as real estate and private equity to maximize return and provide additional portfolio diversification.

The objective of the investment policy for the pension fund is to maintain the funded status of the plan while providing for growth in the plan assets to offset the growth in the plan liabilities. The current target asset allocations are as follows:

Pension Plan Assets	Target
Equity	25%
Fixed Income	59%
Other Investments	15%
Cash and Cash Equivalents	1%

OPEB Plans Assets	Target
Equity	49%
Fixed Income	49%
Cash and Cash Equivalents	2%

The investment policy for each benefit plan contains various investment limitations. The investment policies establish concentration limits for securities and prohibit the purchase of securities issued by AEP (with the exception of proportionate and immaterial holdings of AEP securities in passive index strategies). However, the investment policies do not preclude the benefit trust funds from receiving contributions in the form of AEP securities, provided that the AEP securities acquired by each plan may not exceed the limitations imposed by law.

For equity investments, the concentration limits are as follows:

- No security in excess of 5% of all equities.
- Cash equivalents must be less than 10% of an investment manager's equity portfolio.
- No individual stock may be more than 10% and 7% for pension and OPEB investments, respectively, of each manager's equity portfolio.
- No investment in excess of 5% of an outstanding class of any company.
- No securities may be bought or sold on margin or other use of leverage.

For fixed income investments, each investment manager's portfolio is compared to investment grade, diversified long and intermediate benchmark indices.

A portion of the pension assets is invested in real estate funds to provide diversification, add return and hedge against inflation. Real estate properties are illiquid, difficult to value and not actively traded. The pension plan uses external real estate investment managers to invest in commingled funds that hold real estate properties. To mitigate investment risk in the real estate portfolio, commingled real estate funds are used to ensure that holdings are diversified by region, property type and risk classification. Real estate holdings include core, value-added and opportunistic classifications and some investments in Real Estate Investment Trusts, which are publicly traded real estate securities.

A portion of the pension assets is invested in private equity. Private equity investments add return and provide diversification and typically require a long-term time horizon to evaluate investment performance. Private equity is classified as an alternative investment because it is illiquid, difficult to value and not actively traded. The pension plan uses limited partnerships and commingled funds to invest across the private equity investment spectrum. The private equity holdings are with multiple general partners who help monitor the investments and provide investment selection expertise. The holdings are currently comprised of venture capital, buyout and hybrid debt and equity investment instruments.

AEP participates in a securities lending program with BNY Mellon to provide incremental income on idle assets and to provide income to offset custody fees and other administrative expenses. AEP lends securities to borrowers approved by BNY Mellon in exchange for collateral. All loans are collateralized by at least 102% of the loaned asset's market value and the collateral is invested. The difference between the rebate owed to the borrower and the collateral rate of return determines the earnings on the loaned security. The securities lending program's objective is to provide modest incremental income with a limited increase in risk. As of December 31, 2018 and 2017, the fair value of securities on loan as part of the program was $240.7 million and $491.8 million, respectively. Cash and securities obtained as collateral exceeded the fair value of the securities loaned as of December 31, 2018 and 2017.

Trust owned life insurance (TOLI) underwritten by The Prudential Insurance Company is held in the OPEB plan trusts. The strategy for holding life insurance contracts in the taxable Voluntary Employees' Beneficiary Association trust is to minimize taxes paid on the asset growth in the trust. Earnings on plan assets are tax-deferred within the TOLI contract and can be tax-free if held until claims are paid. Life insurance proceeds remain in the trust and are used to fund future retiree medical benefit liabilities. With consideration to other investments held in the trust, the cash value of the TOLI contracts is invested in two diversified funds. A portion is invested in a commingled fund with underlying investments in stocks that are actively traded on major international equity exchanges. The other portion of the TOLI cash value is invested in a diversified, commingled fixed income fund with underlying investments in government bonds, corporate bonds and asset-backed securities.

Cash and cash equivalents are held in each trust to provide liquidity and meet short-term cash needs. Cash equivalent funds are used to provide diversification and preserve principal. The underlying holdings in the cash funds are investment grade money market instruments including commercial paper, certificates of deposit, treasury bills and other types of investment grade short-term debt securities. The cash funds are valued each business day and provide daily liquidity.

Earnings Per Share (EPS)

AEGCo is a wholly-owned subsidiary of AEP. Therefore, AEGCo is not required to report EPS.

Subsequent Events

Management reviewed subsequent events through February 21, 2019, the date that AEGCo's 2018 annual 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 2014-09 "Revenue from Contracts with Customers" (ASU 2014-09)

In May 2014, the FASB issued ASU 2014-09 changing the method used to determine the timing and requirements for revenue recognition on the statements of income. Under the new standard, an entity must identify the performance obligations in a contract with a customer, determine the transaction price and allocate the price to specific performance obligations to recognize the revenue when the obligation is completed. The amendments in this update also require disclosure of sufficient information to allow users to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

Management adopted ASU 2014-09 effective January 1, 2018, by means of the modified retrospective approach for all contracts within the scope of the new standard. The adoption of ASU 2014-09 did not have a material impact on results of operations, financial position or cash flows. In that regard, the application of the new standard did not cause any significant differences in any individual financial statement line items had those line items been presented in accordance with the guidance that was in effect prior to the adoption of the new standard. Further, given the lack of material impact to the financial statements, the adoption of the new standard did not give rise to any material changes in AEGCo's previously established accounting policies for revenue. See Note 14 - Revenue from Contracts with Customers for additional disclosures required by the new standard.

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. The impact to the balance sheet has been estimated for the first quarter of 2019 as $288.3 million.

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 2017-07 "Compensation - Retirement Benefits" (ASU 2017-07)

In March 2017, the FASB issued ASU 2017-07 requiring that an employer report the service cost component of pension and postretirement benefits in the same line item or items as other compensation costs. The other components of net benefit cost are required to be presented on the statements of income separately from the service cost component and outside of a subtotal of income from operations. In addition, only the service cost component is eligible for capitalization as applicable following labor.

Management adopted ASU 2017-07 effective January 1, 2018. Presentation of the non-service components on a separate line outside of operating income was applied on a retrospective basis, using the amounts disclosed in the benefit plan note for the estimation basis as a practical expedient. Capitalization of only the service cost component was applied on a prospective basis.

ASU 2017-12 "Derivatives and Hedging" (ASU 2017-12)

In August 2017, the FASB issued ASU 2017-12 amending the recognition and presentation requirements for hedge accounting activities. The objectives of the new standard are to improve the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements and to reduce the complexity of applying hedge accounting. Among other things, ASU 2017-12: (a) expands the types of transactions eligible for hedge accounting, (b) eliminates the separate measurement and presentation of hedge ineffectiveness, (c) simplifies the requirements for assessments of hedge effectiveness, (d) provides companies more time to finalize hedge documentation and (e) enhances presentation and disclosure requirements.

Management early adopted ASU 2017-12 in the second quarter of 2018, effective January 1, 2018, by means of a modified retrospective approach. The adoption of ASU 2017-12 did not have an impact on results of operations, financial position or cash flows. The adoption of the new standard did not give rise to any material changes to AEGCo's previously established accounting policies for derivatives and hedging.

ASU 2018-14 "Disclosure Framework: Changes to the Disclosure Requirements for Defined Benefit Plans" (ASU 2018-14)

In August 2018, the FASB issued ASU 2018-14 modifying the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. The amendments in this Update to Subtopic 715-20 remove disclosures that no longer are considered cost beneficial, clarify the specific requirements of disclosures and add disclosure requirements identified as relevant.

Management early adopted ASU 2018-14 for the 2018 Annual Report and applied the new standard retrospectively for all periods presented. As a result of adoption, AEGCo's disclosures were updated as follows:

- Amended the disclosure to remove the amounts in AOCI expected to be recognized as components of net periodic benefit cost over the next fiscal year.
- Amended the disclosure to remove the effects of a one-percentage-point change in assumed health care cost trend rates on the (a) aggregate of the service and interest cost components of net periodic benefit costs and (b) benefit obligation for postretirement health care benefits.
- Amended the disclosure to include the weighted-average interest crediting rates for cash balance plans and other plans with promised interest crediting rates.
- Amended the disclosure to include an explanation of the reasons for significant gains and losses related to changes in the benefit obligation for the period.

See Note 6 - Benefit Plans for updates to the disclosures required by the new standard.

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. EFFECTS OF REGULATION

Regulatory assets and liabilities are comprised of the following items:

Regulatory Assets:	December 31, 2018	2017	Remaining Recovery Period
	(in thousands)		
Noncurrent Regulatory Assets			
Regulatory assets approved for recovery:			
Regulatory Assets Currently Earning a Return			
Asset Retirement Obligation	$ 2,394	$ 2,488	26 years
Total Regulatory Assets Currently Earning a Return	2,394	2,488	
Regulatory Assets Currently Not Earning a Return			
Pension and OPEB Funded Status	10,796	11,097	12 years
Unamortized Loss on Reacquired Debt	1,481	1,500	7 years
Other Regulatory Assets Approved for Recovery	—	780	various
Total Regulatory Assets Currently Not Earning a Return	12,277	13,377	
Total Regulatory Assets Approved for Recovery	14,671	15,865	
Total Noncurrent Regulatory Assets	$ 14,671	$ 15,865	

Regulatory Liabilities:	December 31, 2018	2017	Remaining Refund Period
	(in thousands)		
Noncurrent Regulatory Liabilities and Deferred Investment Tax Credits			
Regulatory liabilities pending final regulatory determination:			
Income Tax Related Regulatory Liabilities (a)			
Excess ADIT Associated with Certain Depreciable Property	$ —	$ 32,730	
Excess ADIT that is Not Subject to Rate Normalization Requirements	—	6,280	
Total Regulatory Liabilities Pending Final Regulatory Determination	—	39,010	
Regulatory liabilities approved for payment:			
Regulatory Liabilities Currently Paying a Return			
Asset Removal Costs	35,106	32,629	(b)
Deferred Investment Tax Credits	7,716	9,686	4 years
Total Regulatory Liabilities Currently Paying a Return	42,822	42,315	
Regulatory Liabilities Currently Not Paying a Return			
UMWA Pension Withdrawal	3,073	—	4 years
Total Regulatory Liabilities Currently Not Paying a Return	3,073	—	
Income Tax Related Regulatory Liabilities (a)			
Excess ADIT Associated with Certain Depreciable Property	34,873	—	(c)
Excess ADIT that is Not Subject to Rate Normalization Requirements	5,142	—	4 years
Income Taxes Subject to Flow Through	4,098	3,348	12 years
Total Income Tax Related Regulatory Liabilities	44,113	3,348	
Total Regulatory Liabilities Approved for Payment	90,008	45,663	
Total Noncurrent Regulatory Liabilities and Deferred Investment Tax Credits	$ 90,008	$ 84,673	

(a) This balance primarily represents regulatory liabilities for excess accumulated deferred income taxes (Excess ADIT) as a result of the reduction in the corporate federal income tax rate from 35% to 21% related to the enactment of Tax Reform. The regulatory liability balance predominately pays a return due to the inclusion of Excess ADIT in rate base. See "Federal Tax Reform" section of Note 8 for additional information.

(b) Relieved as removal costs are incurred.

(c) Refunded using the Average Rate Assumption Method.

4. 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.

COMMITMENTS

In accordance with the accounting guidance for "Commitments", AEGCo had no contractual commitments as of December 31, 2018.

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 bilateral letters of credit for $45.5 million. The letters of credit mature 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 December 31, 2018, there were no material liabilities recorded for any indemnifications.

Lease Obligations

AEGCo leases certain equipment under master lease agreements. See "Master Lease Agreements" section of Note 9 for additional information.

CONTINGENCIES

Insurance and Potential Losses

AEGCo maintains insurance coverage normal and customary for electric utilities, subject to various deductibles. AEGCo also maintains property and casualty insurance that may cover certain physical damage or third-party injuries caused by cyber security incidents. Insurance coverage includes all risks of physical loss or damage to assets, subject to insurance policy conditions and exclusions. Covered property generally includes power plants, substations, facilities and inventories. The insurance programs also generally provide coverage against loss arising from certain claims made by third-parties and are in excess of AEGCo's retentions. Coverage is generally provided by a combination of the protected cell of EIS and/or various industry mutual and/or commercial insurance carriers.

Some potential losses or liabilities may not be insurable or the amount of insurance carried may not be sufficient to meet potential losses and liabilities, including, but not limited to, liabilities relating to a cyber security incident. Future losses or liabilities, if they occur, which are not completely insured, unless recovered from customers, could reduce future net income and cash flows and impact financial condition.

The Comprehensive Environmental Response Compensation and Liability Act (Superfund) and State Remediation

By-products from the generation of electricity include materials such as ash, slag and sludge. Coal combustion by-products, which constitute the overwhelming percentage of these materials, are typically treated and deposited in captive disposal facilities or are beneficially utilized. In addition, the generation plants and transmission facilities have used asbestos, polychlorinated biphenyls and other hazardous and non-hazardous materials. AEGCo currently incurs costs to dispose of these substances safely.

Superfund addresses clean-up of hazardous substances that are released to the environment. The Federal EPA administers the clean-up programs. Several states enacted similar laws. Superfund does not recognize compliance as a defense, but imposes strict liability on parties who fall within its broad statutory categories. Present estimates do not anticipate material clean-up costs.

Rockport Plant Litigation

In July 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 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.

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.

In July 2017, 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 to eliminate the obligation to install certain future controls at Rockport Plant, Unit 2 if AEP does not acquire ownership of that Unit, and to modify the consent decree in other respects to preserve the environmental benefits of the consent decree. Responsive and supplemental filings have been made by all parties. In November 2017, 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.

Rockport Plant, Unit 2 Selective Catalytic Reduction (SCR)

In 2016, I&M filed an application with the Indiana Utility Regulatory Commission (IURC) for approval of a Certificate of Public Convenience and Necessity (CPCN) to install SCR technology at Rockport Plant, Unit 2. The equipment will allow I&M to reduce emissions of NO_x from Rockport Plant, Unit 2 in order for I&M to continue to operate that unit under current environmental requirements and is expected to be placed in service in May 2020. The estimated cost of the SCR project is $274 million, excluding AFUDC, to be shared equally between I&M and AEGCo. The AEGCo ownership share of the SCR project will be billable under the Rockport Plant UPA to I&M and KPCo and will be subject to future regulatory approval for recovery. In March 2018, the IURC issued an order approving the CPCN and the $274 million estimated cost of the SCR, excluding AFUDC.

5. DISPOSITION

Lawrenceburg Plant

In September 2016, AEP signed a Purchase and Sale Agreement to sell AEGCo's Lawrenceburg Plant as well as other affiliated plants totaling 5,329 MWs of competitive generation assets as one disposal group to a nonaffiliated party. The sale closed in January 2017 for $2.2 billion, of which $726.3 million related to AEGCo's Lawrenceburg Plant were recorded in Investing Activities on AEGCo's statement of cash flows. The net proceeds from the transaction were $363.1 million in cash after taxes, repayment of debt associated with this plant including a make whole payment related to the debt and transaction fees. The sale resulted in a pretax gain of $355.6 million that was recorded in Gain on Sale of Lawrenceburg Plant on AEGCo's statement of income for the year ended December 31, 2017. The Income before Income Tax Expense of the plant was $3.8 million (excluding the $355.6 million pretax gain) for the year ended December 31, 2017.

6. BENEFIT PLANS

For a discussion of investment strategy, investment limitations, target asset allocations and the classification of investments within the fair value hierarchy, see "Fair Value Measurements of Assets and Liabilities" and "Investments Held in Trust for Future Liabilities" sections of Note 1.

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.

AEGCo recognizes its funded status associated with defined benefit pension and OPEB plans on its balance sheets. Disclosures about the plans are required by the "Compensation - Retirement Benefits" accounting guidance. AEGCo recognizes an asset for a plan's overfunded status or a liability for a plan's underfunded status and recognizes, as a component of other comprehensive income, the changes in the funded status of the plan that arise during the year that are not recognized as a component of net periodic benefit cost. AEGCo records a regulatory asset instead of other comprehensive income for qualifying benefit costs of regulated operations that for ratemaking purposes are deferred for future recovery. The cumulative funded status adjustment is equal to the remaining unrecognized deferrals for unamortized actuarial losses or gains, prior service costs and transition obligations, such that remaining deferred costs result in a regulatory asset and deferred gains result in a regulatory liability.

Actuarial Assumptions for Benefit Obligations

The weighted-average assumptions used in the measurement of benefit obligations are shown in the following table:

	Pension Plan		OPEB	
	December 31,			
Assumption	**2018**	**2017**	**2018**	**2017**
Discount Rate	4.30%	3.65%	4.30%	3.60%
Interest Crediting Rate	4.00%	4.00%	NA	NA
Rate of Compensation Increase	5.75% (a)	5.85% (a)	NA	NA

(a) Rates are for base pay only. In addition, an amount is added to reflect target incentive compensation for exempt employees and overtime and incentive pay for nonexempt employees.
NA Not applicable.

A duration-based method is used to determine the discount rate for the plans. A hypothetical portfolio of high quality corporate bonds is constructed with cash flows matching the benefit plan liability. The composite yield on the hypothetical bond portfolio is used as the discount rate for the plan.

For 2018, the rate of compensation increase assumed varies with the age of the employee, ranging from 3.5% per year to 12% per year, with an average increase of 5.75%.

Actuarial Assumptions for Net Periodic Benefit Costs

The weighted-average assumptions used in the measurement of benefit costs are shown in the following table:

	Pension Plan		OPEB	
	Year Ended December 31,			
Assumption	**2018**	**2017**	**2018**	**2017**
Discount Rate	3.65%	4.05%	3.60%	4.10%
Interest Crediting Rate	4.00%	4.00%	NA	NA
Expected Return on Plan Assets	6.00%	6.00%	6.00%	6.75%
Rate of Compensation Increase	5.75% (a)	5.85% (a)	NA	NA

(a) Rates are for base pay only. In addition, an amount is added to reflect target incentive compensation for exempt employees and overtime and incentive pay for nonexempt employees.
NA Not applicable.

The expected return on plan assets was determined by evaluating historical returns, the current investment climate (yield on fixed income securities and other recent investment market indicators), rate of inflation, third party forecasts and current prospects for economic growth.

The health care trend rate assumptions used for OPEB plans measurement purposes are shown below:

	December 31,	
Health Care Trend Rates	**2018**	**2017**
Initial	6.25%	6.50%
Ultimate	5.00%	5.00%
Year Ultimate Reached	2024	2024

Significant Concentrations of Risk within Plan Assets

In addition to establishing the target asset allocation of plan assets, the investment policy also places restrictions on securities to limit significant concentrations within plan assets. The investment policy establishes guidelines that govern maximum market exposure, security restrictions, prohibited asset classes, prohibited types of transactions, minimum credit quality, average portfolio credit quality, portfolio duration and concentration limits. The guidelines were established to mitigate the risk of loss due to significant concentrations in any investment. The plans are monitored to control security diversification and ensure compliance with the investment policy. As of December 31, 2018, the assets were invested in compliance with all investment limits. See "Investments Held in Trust for Future Liabilities" section of Note 1 for limit details.

Benefit Plan Obligations, Plan Assets and Funded Status

For the year ended December 31, 2018, the pension and OPEB plans had an actuarial gain due to an increase in the discount rate as well as updated estimates for future medical expenses in the OPEB plans. For the year ended December 31, 2017, the pension and OPEB plans had an actuarial loss due to a decrease in the discount rate as well as updated estimates for future medical expenses in the OPEB plans. The following table provides a reconciliation of the changes in the plans' benefit obligations, fair value of plan assets and funded status. The benefit obligation for the defined benefit pension and OPEB plans are the projected benefit obligation and the accumulated benefit obligation, respectively.

	Pension Plan		OPEB	
	2018	**2017**	**2018**	**2017**
Change in Benefit Obligation	(in thousands)			
Benefit Obligation as of January 1,	$ 3,862	$ 3,652	$ 49,374	$ 43,490
Service Cost	84	75	1,162	858
Interest Cost	118	147	2,017	1,684
Actuarial (Gain) Loss	(868)	166	(4,274)	4,226
Benefit Payments	(187)	(178)	(1,434)	(1,025)
Participant Contributions	—	—	33	52
Medicare Subsidy	—	—	99	89
Benefit Obligation as of December 31,	$ 3,009	$ 3,862	$ 46,977	$ 49,374
Change in Fair Value of Plan Assets				
Fair Value of Plan Assets as of January 1,	$ 4,526	$ 4,172	$ 38,378	$ 32,788
Actual Gain (Loss) on Plan Assets	(92)	525	(2,460)	5,707
Company Contributions	—	7	1,319	856
Participant Contributions	—	—	33	52
Benefit Payments	(187)	(178)	(1,434)	(1,025)
Fair Value of Plan Assets as of December 31,	$ 4,247	$ 4,526	$ 35,836	$ 38,378
Funded (Underfunded) Status as of December 31,	$ 1,238	$ 664	$ (11,141)	$ (10,996)

Amounts Recognized on the Balance Sheets

	Pension Plan				OPEB			
	December 31,							
	2018		2017		2018		2017	
	(in thousands)							
Deferred Charges and Other Noncurrent Assets – Prepaid Benefit Costs	$	1,238	$	664	$	275	$	446
Deferred Credits and Other Noncurrent Liabilities – Accrued Long-term Benefit Liability		—		—		(11,416)		(11,442)
Funded (Underfunded) Status	$	1,238	$	664	$	(11,141)	$	(10,996)

Amounts Included in Regulatory Assets

The following table shows the components of the plans included in Regulatory Assets:

	Pension Plan				OPEB			
	December 31,							
	2018		2017		2018		2017	
Components	(in thousands)							
Net Actuarial (Gain) Loss	$	(789)	$	(215)	$	11,927	$	11,722
Prior Service Credit		—		—		(342)		(410)
Recorded as								
Regulatory Assets	$	(789)	$	(215)	$	11,585	$	11,312

Components of the change in amounts included in Regulatory Assets were as follows:

	Pension Plan				OPEB			
	2018		2017		2018		2017	
Components	(in thousands)							
Actuarial (Gain) Loss During the Year	$	(522)	$	(113)	$	926	$	725
Amortization of Actuarial Loss		(52)		(59)		(721)		(376)
Amortization of Prior Service Credit (Cost)		—		(1)		68		68
Change for the Year Ended December 31,	$	(574)	$	(173)	$	273	$	417

Determination of Pension Expense

The determination of pension expense or income is based on a market-related valuation of assets which reduces year-to-year volatility. This market-related valuation recognizes investment gains or losses over a five-year period from the year in which they occur. Investment gains or losses for this purpose are the difference between the expected return calculated using the market-related value of assets and the actual return.

Pension and OPEB Assets

The fair value tables within Pension and OPEB Assets present the classification of assets for AEP within the fair value hierarchy. All Level 1, 2, 3 and Other amounts can be allocated to AEGCo using the percentages in the table below:

Pension Plan		OPEB	
December 31,			
2018	2017	2018	2017
0.1%	0.1%	2.3%	2.2%

The following table presents the classification of pension plan assets for AEP within the fair value hierarchy as of December 31, 2018:

Asset Class	Level 1	Level 2	Level 3	Other	Total	Year End Allocation
			(in millions)			
Equities (a):						
Domestic	$ 277.3	$ —	$ —	$ —	$ 277.3	5.9%
International	384.1	—	—	—	384.1	8.2%
Options	—	18.3	—	—	18.3	0.4%
Common Collective Trusts (c)	—	—	—	370.1	370.1	7.9%
Subtotal – Equities	661.4	18.3	—	370.1	1,049.8	22.4%
Fixed Income (a):						
United States Government and Agency Securities	0.2	1,512.5	—	—	1,512.7	32.2%
Corporate Debt	—	1,082.9	—	—	1,082.9	23.0%
Foreign Debt	—	221.6	—	—	221.6	4.7%
State and Local Government	—	28.2	—	—	28.2	0.6%
Other – Asset Backed	—	7.4	—	—	7.4	0.2%
Subtotal – Fixed Income	0.2	2,852.6	—	—	2,852.8	60.7%
Infrastructure (c)	—	—	—	72.2	72.2	1.5%
Real Estate (c)	—	—	—	220.4	220.4	4.7%
Alternative Investments (c)	—	—	—	444.6	444.6	9.5%
Cash and Cash Equivalents (c)	(0.4)	36.3	—	11.9	47.8	1.0%
Other – Pending Transactions and Accrued Income (b)	—	—	—	8.3	8.3	0.2%
Total	$ 661.2	$ 2,907.2	$ —	$ 1,127.5	$ 4,695.9	100.0%

(a) Includes investment securities loaned to borrowers under the securities lending program. See the "Investments Held in Trust for Future Liabilities" section of Note 1 for additional information.
(b) Amounts in "Other" column primarily represent accrued interest, dividend receivables and transactions pending settlement.
(c) Amounts in "Other" column represent investments for which fair value is measured using net asset value per share.

The following table presents the classification of OPEB plan assets for AEP within the fair value hierarchy as of December 31, 2018:

Asset Class	Level 1	Level 2	Level 3	Other	Total	Year End Allocation
			(in millions)			
Equities:						
Domestic	$ 233.3	$ —	$ —	$ —	$ 233.3	15.2 %
International	185.9	—	—	—	185.9	12.1 %
Options	—	4.3	—	—	4.3	0.3 %
Common Collective Trusts (b)	—	—	—	226.2	226.2	14.7 %
Subtotal – Equities	419.2	4.3	—	226.2	649.7	42.3 %
Fixed Income:						
Common Collective Trust – Debt (b)	—	—	—	163.6	163.6	10.7 %
United States Government and Agency Securities	0.2	181.5	—	—	181.7	11.8 %
Corporate Debt	—	188.6	—	—	188.6	12.3 %
Foreign Debt	—	35.0	—	—	35.0	2.3 %
State and Local Government	41.8	11.8	—	—	53.6	3.5 %
Other – Asset Backed	—	0.2	—	—	0.2	— %
Subtotal – Fixed Income	42.0	417.1	—	163.6	622.7	40.6 %
Trust Owned Life Insurance:						
International Equities	—	49.4	—	—	49.4	3.2 %
United States Bonds	—	154.4	—	—	154.4	10.1 %
Subtotal – Trust Owned Life Insurance	—	203.8	—	—	203.8	13.3 %
Cash and Cash Equivalents (b)	54.4	—	—	4.8	59.2	3.9 %
Other – Pending Transactions and Accrued Income (a)	—	—	—	(1.2)	(1.2)	(0.1)%
Total	$ 515.6	$ 625.2	$ —	$ 393.4	$ 1,534.2	100.0 %

(a) Amounts in “Other” column primarily represent accrued interest, dividend receivables and transactions pending settlement.
(b) Amounts in “Other” column represent investments for which fair value is measured using net asset value per share.

The following table presents the classification of pension plan assets for AEP within the fair value hierarchy as of December 31, 2017:

Asset Class	Level 1	Level 2	Level 3	Other	Total	Year End Allocation
			(in millions)			
Equities (a):						
Domestic	$ 318.6	$ —	$ —	$ —	$ 318.6	6.2%
International	507.7	—	—	—	507.7	9.8%
Options	—	26.9	—	—	26.9	0.5%
Common Collective Trusts (c)	—	—	—	452.9	452.9	8.7%
Subtotal – Equities	826.3	26.9	—	452.9	1,306.1	25.2%
Fixed Income (a):						
United States Government and Agency Securities	—	1,376.5	—	—	1,376.5	26.6%
Corporate Debt	—	1,277.0	—	—	1,277.0	24.7%
Foreign Debt	—	296.9	—	—	296.9	5.7%
State and Local Government	—	31.7	—	—	31.7	0.6%
Other – Asset Backed	—	10.2	—	—	10.2	0.2%
Subtotal – Fixed Income	—	2,992.3	—	—	2,992.3	57.8%
Infrastructure (c)	—	—	—	59.5	59.5	1.2%
Real Estate (c)	—	—	—	290.3	290.3	5.6%
Alternative Investments (c)	—	—	—	446.0	446.0	8.6%
Cash and Cash Equivalents (c)	0.4	35.6	—	21.2	57.2	1.1%
Other – Pending Transactions and Accrued Income (b)	—	—	—	22.7	22.7	0.5%
Total	$ 826.7	$ 3,054.8	$ —	$ 1,292.6	$ 5,174.1	100.0%

(a) Includes investment securities loaned to borrowers under the securities lending program. See the "Investments Held in Trust for Future Liabilities" section of Note 1 for additional information.
(b) Amounts in "Other" column primarily represent accrued interest, dividend receivables and transactions pending settlement.
(c) Amounts in "Other" column represent investments for which fair value is measured using net asset value per share.

The following table sets forth a reconciliation of changes for in the fair value of AEP's assets classified as Level 3 in the fair value hierarchy for the pension assets:

	Infrastructure	Real Estate	Alternative Investments	Total Level 3
		(in millions)		
Balance as of January 1, 2017	$ 57.6	$ 254.9	$ 411.1	$ 723.6
Actual Return on Plan Assets				
Relating to Assets Still Held as of the Reporting Date	—	—	—	—
Relating to Assets Sold During the Period	—	—	—	—
Purchases and Sales	—	—	—	—
Transfers into Level 3	—	—	—	—
Transfers out of Level 3 (a)	(57.6)	(254.9)	(411.1)	(723.6)
Balance as of December 31, 2017	$ —	$ —	$ —	$ —

(a) The classification of Level 3 assets from the prior year was corrected in the current year presentation and included within the fair value hierarchy table as of December 31, 2017 as "Other" investments for which fair value is measured using net asset value per share in accordance with ASU 2015-07, Disclosure for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent). Management concluded that these disclosure errors were immaterial individually and in the aggregate to all prior periods presented.

The following table presents the classification of OPEB plan assets for AEP within the fair value hierarchy as of December 31, 2017:

Asset Class	Level 1	Level 2	Level 3	Other	Total	Year End Allocation
			(in millions)			
Equities:						
Domestic	$ 307.1	$ —	$ —	$ —	$ 307.1	17.7 %
International	306.9	—	—	—	306.9	17.7 %
Options	—	9.4	—	—	9.4	0.5 %
Common Collective Trusts (b)	—	—	—	153.6	153.6	8.9 %
Subtotal – Equities	614.0	9.4	—	153.6	777.0	44.8 %
Fixed Income:						
Common Collective Trust – Debt (b)	—	—	—	185.0	185.0	10.7 %
United States Government and Agency Securities	—	187.4	—	—	187.4	10.8 %
Corporate Debt	—	214.1	—	—	214.1	12.4 %
Foreign Debt	—	40.7	—	—	40.7	2.4 %
State and Local Government	49.7	16.8	—	—	66.5	3.8 %
Other – Asset Backed	—	0.2	—	—	0.2	— %
Subtotal – Fixed Income	49.7	459.2	—	185.0	693.9	40.1 %
Trust Owned Life Insurance:						
International Equities	—	105.4	—	—	105.4	6.1 %
United States Bonds	—	118.2	—	—	118.2	6.8 %
Subtotal – Trust Owned Life Insurance	—	223.6	—	—	223.6	12.9 %
Cash and Cash Equivalents (b)	36.7	—	—	4.2	40.9	2.4 %
Other – Pending Transactions and Accrued Income (a)	—	—	—	(2.9)	(2.9)	(0.2)%
Total	$ 700.4	$ 692.2	$ —	$ 339.9	$ 1,732.5	100.0 %

(a) Amounts in "Other" column primarily represent accrued interest, dividend receivables and transactions pending settlement.
(b) Amounts in "Other" column represent investments for which fair value is measured using net asset value per share.

Accumulated Benefit Obligation

As of December 31, 2018 and 2017, the accumulated benefit obligation for the qualified pension plan was $2.8 million and $3.6 million, respectively.

Estimated Future Benefit Payments and Contributions

AEGCo expects contributions and payments for the OPEB plans of $875 thousand during 2019. Contributions to the pension trust, when needed, are at least the minimum amount required by the Employee Retirement Income Security Act and additional discretionary contributions may also be made to maintain the funded status of the plan.

The table below reflects the total benefits expected to be paid from the plan or from AEGCo's assets. The payments include the participants' contributions to the plan for their share of the cost. Future benefit payments are dependent on the number of employees retiring, whether the retiring employees elect to receive pension benefits as annuities or as lump sum distributions, future integration of the benefit plans with changes to Medicare and other legislation, future levels of interest rates and variances in actuarial results. The estimated payments for pension benefits and OPEB are as follows:

	Pension Plan	OPEB	
	Pension Payments	Benefit Payments	Medicare Subsidy Receipts
		(in thousands)	
2019	$ 176	$ 1,281	$ 38
2020	174	1,282	50
2021	171	1,337	58
2022	168	1,418	68
2023	166	1,494	77
Years 2024 to 2028, in Total	865	8,503	509

Components of Net Periodic Benefit Cost

The following table provides the components of net periodic benefit cost:

	Pension Plan		OPEB	
	Years Ended December 31,			
	2018	2017	2018	2017
		(in thousands)		
Service Cost	$ 84	$ 75	$ 1,162	$ 858
Interest Cost	118	147	2,017	1,684
Expected Return on Plan Assets	(254)	(246)	(2,739)	(2,206)
Amortization of Prior Service Cost (Credit)	—	1	(68)	(68)
Amortization of Net Actuarial Loss	52	59	721	376
Net Periodic Benefit Cost	$ —	$ 36	$ 1,093	$ 644

American Electric Power System Retirement Savings Plan

AEGCo participates in an AEP sponsored defined contribution retirement savings plan, the American Electric Power System Retirement Savings Plan, for substantially all employees who are not covered by a retirement savings plan of the UMWA. This qualified plan offers participants an opportunity to contribute a portion of their pay, includes features under Section 401(k) of the Internal Revenue Code and provides for matching contributions. The matching contributions to the plan are 100% of the first 1% of eligible employee contributions and 70% of the next 5% of contributions. The cost for matching contributions totaled $86 thousand in 2018 and $60 thousand in 2017.

UMWA Benefits

Health and Welfare Benefits

AEGCo provides health and welfare benefits for certain unionized employees, retirees and their survivors who meet eligibility requirements. AEGCo administers the health and welfare benefits and pays them from its general assets.

Multiemployer Pension Benefits

UMWA pension benefits are provided through the United Mine Workers of America 1974 Pension Plan (Employer Identification Number: 52-1050282, Plan Number 002), a multiemployer plan. The UMWA pension benefits are administered by a board of trustees appointed in equal numbers by the UMWA and the Bituminous Coal Operators' Association (BCOA), an industry bargaining association. AEGCo makes contributions to the United Mine Workers of America 1974 Pension Plan based on provisions in its labor agreement and the plan documents. The UMWA pension plan is different from single-employer plans as an employer's contributions may be used to provide benefits to employees of other participating employers. A withdrawing employer may be subject to a withdrawal liability, which is calculated based upon that employer's share of the plan's unfunded benefit obligations. If an employer fails to make required contributions or if its payments in connection with its withdrawal liability fall short of satisfying its share of the plan's unfunded benefit obligations, the remaining employers may be allocated a greater share of the remaining unfunded plan obligations. Under the Pension Protection Act of 2006 (PPA), the UMWA pension plan was in Critical and Declining Status for the plan years ending June 30, 2018 and 2017, without utilization of extended amortization provisions. As required under the PPA, the Plan adopted a Rehabilitation Plan in February 2015 which was updated in 2016, 2017 and April 2018.

The amounts contributed in 2018 and 2017 were $617 thousand and $483 thousand, respectively, and represent less than 5% of the total contributions in the plan's latest annual report based on the plan year ended June 30, 2017. The contributions in 2018 and 2017 did not include surcharges.

Under the terms of the UMWA pension plan, contributions will be required to continue beyond the December 31, 2020 expiration of the current collective bargaining agreement, whether or not the term of that agreement is extended or a subsequent agreement is entered, so long as both the UMWA pension plan remains in effect and AEGCo continues to operate the CCT facility covered by the current collective bargaining agreement. The contribution rate applicable would be determined in accordance with the terms of the UMWA pension plan by reference to the National Bituminous Coal Wage Agreement, subject to periodic revisions, between the UMWA and the BCOA. If the UMWA pension plan would terminate or AEGCo would cease operation of the CCT facility without arranging for a successor operator to assume its liability, the withdrawal liability obligation would be triggered.

Based upon the planned closure of the CCT facility in 2022, AEGCo records a UMWA pension withdrawal liability on the balance sheet. The UMWA pension withdrawal liability is re-measured annually and is the estimated value of the company's proportionate share of the plan's unfunded vested liabilities. As of December 31, 2018 and 2017, the liability balance was $15.2 million and $18.6 million, respectively. AEGCo recovers the estimated UMWA pension withdrawal liability through billings for transloading services to regulated affiliates. A regulatory asset is recorded on the balance sheet when the UMWA pension withdrawal liability exceeds the cumulative billings collected from regulated affiliates and a regulatory liability on the balance sheets when the cumulative billings collected exceed the withdrawal liability. As of December 31, 2018 AEGCo recorded a regulatory liability on the balance sheets for $3.1 million and as of December 31, 2017, AEGCo recorded a regulatory asset on the balance sheets for $509 thousand, respectively. If any portion of the UMWA pension withdrawal liability is not recovered from regulated affiliates, it could reduce AEGCo's future net income and cash flows and impact financial condition.

7. FAIR VALUE MEASUREMENTS

Fair Value Measurements of Long-term Debt

For a discussion of fair value accounting and the classification of assets and liabilities within the fair value hierarchy, see the "Fair Value Measurements of Assets and Liabilities" section of Note 1.

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:

	December 31,			
	2018		2017	
	Book Value	Fair Value	Book Value	Fair Value
	(in thousands)			
Long-term Debt	$ 194,988	$ 195,000	$ 169,891	$ 170,000

8. INCOME TAXES

Federal Tax Reform and Legislation

In December 2017, Tax Reform legislation was signed into law. Tax Reform includes significant changes to the Internal Revenue Code of 1986, as amended, including lowering the corporate federal income tax rate from 35% to 21%. As a result of this rate change, AEGCo's deferred tax assets and liabilities were remeasured using the newly enacted rate of 21% in December 2017. In response to Tax Reform, the SEC staff issued Staff Accounting Bulletin 118 (SAB 118) in December 2017. SAB 118 provided for up to a one year period (the measurement period) in which to complete the required analyses and accounting required by Tax Reform.

During 2017, AEGCo recorded provisional amounts for the income tax effects of Tax Reform. Throughout 2018, AEGCo continued to assess the impacts of legislative changes in the tax code as well as interpretative changes of the tax code. The measurement period adjustments recorded during 2018 were immaterial.

The measurement period under SAB 118 ended in December 2018. However, Tax Reform uncertainties still remain and AEGCo will continue to monitor income tax effects that may change as a result of future legislation and further interpretation of Tax Reform based on proposed U.S. Treasury regulations and guidance from the IRS and state tax authorities.

Federal Legislation

The IRS has proposed new regulations that provide guidance regarding the additional first-year depreciation deduction under Section 168(k). The proposed regulations reflect changes as a result of Tax Reform and affect taxpayers with qualified depreciable property acquired and placed in service after September 27, 2017. Generally, AEGCo's regulated businesses will not be eligible for any bonus depreciation for property acquired and placed in service after January 1, 2018. However, for self-constructed property and other property placed in service in 2018 for which construction began prior to January 1, 2018, taxpayers are required to evaluate the contractual terms to determine if these additions qualify for 100% expensing under Tax Reform or 50% bonus depreciation as provided under prior tax law.

Excess Accumulated Deferred Income Taxes (Excess ADIT)

As reflected in AEGCo's annual ETR for 2018, AEGCo began amortizing the Excess ADIT associated with certain depreciable property using the average rate assumption method during the first quarter of 2018. The benefit associated with the amortization of the Excess ADIT was passed through to AEP affiliates through CCT and Rockport UPA billings. In February 2019, the FERC issued an order approving the amortization of Excess ADIT that is not subject to rate normalization requirements over 4 years to begin in January 2019.

Income Tax Expense (Benefit)

The details of AEGCo's Income Tax Expense (Benefit) are as follows:

	Years Ended December 31, 2018	2017
	(in thousands)	
Federal:		
Current	$ (9,457)	$ 125,424
Deferred	2,554	(18,866)
Deferred Investment Tax Credits	(1,970)	(1,969)
Total Federal	(8,873)	104,589
State and Local:		
Current	2,095	9,963
Deferred	(58)	(24)
Total State and Local	2,037	9,939
Income Tax Expense (Benefit)	$ (6,836)	$ 114,528

The following is a reconciliation between the federal income taxes computed by multiplying pretax income by the federal statutory tax rate and the income taxes reported:

	Years Ended December 31, 2018	2017
	(in thousands)	
Net Income	$ 30,438	$ 271,458
Income Tax Expense (Benefit)	(6,836)	114,528
Pretax Income	$ 23,602	$ 385,986
Income Taxes on Pretax Income at Statutory Rate (21% and 35% in 2018 and 2017, Respectively)	$ 4,956	$ 135,095
Increase (Decrease) in Income Taxes Resulting from the Following Items:		
Depreciation	2,539	2,580
Plant Sales	—	(26,705)
Investment Tax Credit Amortization	(1,970)	(1,969)
State and Local Income Taxes, Net	1,609	6,460
Tax Reform	—	—
Tax Reform Excess ADIT Reversal	(586)	—
Parent Savings	(12,930)	(3,838)
Other	(454)	2,905
Income Tax Expense (Benefit)	$ (6,836)	$ 114,528
Effective Income Tax Rate	(29.0)%	29.7 %

Net Deferred Tax Liability

The following table shows elements of AEGCo's net deferred tax liability and significant temporary differences:

	December 31, 2018	December 31, 2017
	(in thousands)	
Deferred Tax Assets	$ 28,020	$ 41,645
Deferred Tax Liabilities	(58,892)	(71,776)
Net Deferred Tax Liabilities	$ (30,872)	$ (30,131)
Property Related Temporary Differences	$ (47,434)	$ (43,771)
Amounts Due To Customers for Future Federal Income Taxes	8,004	9,282
Deferred State Income Taxes	(1,195)	(1,598)
Net Deferred Gain on Sale-and-Leaseback – Rockport Plant, Unit 2	4,601	5,870
Postretirement Benefits	2,985	4,290
All Other, Net	2,167	(4,204)
Net Deferred Tax Liabilities	$ (30,872)	$ (30,131)

AEP System Tax Allocation Agreement

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

Federal and State Income Tax Audit Status

AEGCo and other AEP subsidiaries are no longer subject to U.S. federal examination for years before 2011. The IRS examination of years 2011 through 2013 started in April 2014. AEGCo and other AEP subsidiaries received a Revenue Agents Report in April 2016, completing the 2011 through 2013 audit cycle indicating an agreed upon audit. The 2011 through 2013 audit was submitted to the Congressional Joint Committee on Taxation for approval. The Joint Committee referred the audit back to the IRS exam team for further consideration. To resolve the issue under consideration, AEGCo and other AEP subsidiaries and the IRS exam team agreed to utilize the Fast Track Settlement Program in December 2017. The program was completed in March 2018 and tax years 2014 and 2015 were added to the IRS examination to reflect the impact of the Fast Track changes that were carried forward to 2014 and 2015. In June 2018, AEGCo and other AEGCo and other AEP subsidiaries settled all outstanding issues under audit for tax years 2011-2015. The Joint Committee approved the settlement in November 2018. The settlement did not materially impact AEGCo's net income, cash flows or financial condition. The IRS examination of 2016 began in October 2018.

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.

Uncertain Tax Positions

The reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

	2018	2017
	(in thousands)	
Balance as of January 1,	$ 4,928	$ 4,928
Increase – Tax Positions Taken During a Prior Period	—	—
Decrease – Tax Positions Taken During a Prior Period	—	—
Increase – Tax Positions Taken During the Current Year	—	—
Decrease – Tax Positions Taken During the Current Year	—	—
Increase – Settlements with Taxing Authorities	—	—
Decrease – Settlements with Taxing Authorities	—	—
Decrease – Lapse of the Applicable Statute of Limitations	—	—
Balance as of December 31,	$ 4,928	$ 4,928

Management believes that there will be no significant net increase or decrease in unrecognized benefits within 12 months of the reporting date. The total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate is $3.2 million for 2018 and 2017.

State Tax Legislation

In June 2018, the United States Supreme Court issued a decision which eliminated a physical presence requirement for the imposition of sales and use tax and instead applied an economic nexus concept. Although this case was specific to sales and use taxes, many states are beginning to consider whether they could also apply this economic nexus concept to income taxes. Management continues to monitor state legislation to determine whether it could create any income tax liability in any states in which AEGCo currently does not file.

9. LEASES

Leases of property, plant and equipment are for remaining periods up to 6 years and require payments of related property taxes, maintenance and operating costs. The majority of the leases have purchase or renewal options and will be renewed or replaced by other leases.

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

Lease Rental Costs	Years Ended December 31, 2018	2017
	(in thousands)	
Net Lease Expense on Operating Leases	$ 72,960	$ 72,960
Amortization of Capital Leases	1,800	1,880
Interest on Capital Leases	1,519	1,642
Total Lease Rental Costs	$ 76,279	$ 76,482

The following table shows the property, plant and equipment under capital leases and related obligations recorded on AEGCo's balance sheets. Capital lease obligations are included in Other Current Liabilities and Deferred Credits and Other Noncurrent Liabilities on AEGCo's balance sheets.

	December 31, 2018	2017
	(in thousands)	
Property, Plant and Equipment Under Capital Leases		
Generation	$ 25,370	$ 25,906
Other Property, Plant and Equipment	1,448	1,459
Total Property, Plant and Equipment Under Capital Leases	26,818	27,365
Accumulated Amortization	8,553	7,494
Net Property, Plant and Equipment Under Capital Leases	$ 18,265	$ 19,871
Obligations Under Capital Leases		
Noncurrent Liability	$ 16,413	$ 18,101
Liability Due Within One Year	1,852	1,770
Total Obligations Under Capital Leases	$ 18,265	$ 19,871

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

Future Minimum Lease Payments	Capital Leases	Noncancelable Operating Leases
	(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	24,201	$ 313,034
Less Estimated Interest Element	5,936	
Estimated Present Value of Future Minimum Lease Payments	$ 18,265	

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 either the unamortized balance or the equipment cost at the end of the lease term. If the actual fair value of the leased equipment is below the guaranteed residual value at the end of the lease term, 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 unamortized balance. As of December 31, 2018, 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.

The gain from the sale was deferred and is being amortized over the term of the lease, which expires in 2022. The Owner Trustee owns the Plant and leases it 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 or the Owner Trustee can sell the Plant. 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 December 31, 2018 were as follows:

Future Minimum Lease Payments	**(in thousands)**
2019	$ 73,854
2020	73,854
2021	73,854
2022	73,854
Total Future Minimum Lease Payments	$ 295,416

10. FINANCING ACTIVITIES

Long-term Debt

The following table details long-term debt outstanding:

Type of Debt	Maturity	Weighted-Average Interest Rate as of December 31, 2018	Interest Rate as of December 31, 2018	Interest Rate as of December 31, 2017	Outstanding as of December 31, 2018	Outstanding as of December 31, 2017
					(in thousands)	
Pollution Control Bonds (a)	2018-2019 (b)	1.68%	1.68%	1.59%-1.60%	$ 45,000	$ 44,998
Other Long-term Debt	2018-2020	3.10%	3.10%	2.35%	149,988	124,893
Total Long-term Debt Outstanding					$ 194,988	$ 169,891

(a) For AEGCo's Pollution Control Bonds, interest rates are subject to periodic adjustment and may be purchased on demand at periodic interest adjustment dates.

(b) AEGCo's Pollution Control Bonds are subject to redemption earlier than the maturity date. Consequently, these bonds have been classified for maturity purposes as Long-term Debt Due Within One Year - Nonaffiliated on AEGCo's balance sheets.

As of December 31, 2018, outstanding long-term debt was payable as follows:

	2019	2020	2021	2022	2023	After 2023	Total
				(in thousands)			
Principal Amount	$ 45,000	$ 150,000	$ —	$ —	$ —	$ —	$ 195,000
Debt Issuance Costs							(12)
Total Long-term Debt Outstanding							$ 194,988

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 December 31, 2018, AEGCo did not exceed its debt to capitalization limit. The method for calculating outstanding debt and capitalization is contractually-defined in the credit agreements.

As of December 31, 2018, the maximum amount of restricted net assets of AEGCo that may not be distributed to Parent in the form of a loan, advance or dividend was $102.4 million.

The credit agreement covenant restrictions can limit the ability of AEGCo to pay dividends out of retained earnings. As of December 31, 2018, there were no restrictions on AEGCo's ability 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 the AEP System Utility Money Pool agreement filed with the FERC. The amounts of outstanding loans to the Utility Money Pool as of December 31, 2018 and 2017 are included in Advances to Affiliates on AEGCo's balance sheets. AEGCo's Utility Money Pool activity and corresponding authorized borrowing limits are described in the following table:

Years Ended December 31,	Maximum Borrowings from the Utility Money Pool	Maximum Loans to the Utility Money Pool	Average Borrowings from the Utility Money Pool	Average Loans to the Utility Money Pool	Loans to the Utility Money Pool as of December 31,	Authorized Short-Term Borrowing Limit
			(in thousands)			
2018	$ —	$ 158,809	$ —	$ 121,341	$ 70,904	$ 200,000
2017	12,217	787,348	12,217	208,052	94,165	200,000

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

Years Ended December 31,	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
2018	—%	—%	2.97%	1.81%	—%	2.18%
2017	1.00%	1.00%	1.85%	0.92%	1.00%	1.23%

Interest expense and interest income related to the Utility Money Pool are included in Interest Expense and Interest Income, respectively, on AEGCo's statements of income. For amounts borrowed from and advances to the Utility Money Pool, AEGCo incurred the following amounts of interest expense and earned the following amounts of interest income:

	Years Ended December 31,	
	2018	2017
	(in thousands)	
Interest Expense	$ —	$ 1
Interest Income	2,692	2,549

11. RELATED PARTY TRANSACTIONS

For other related party transactions, also see "AEP System Tax Allocation Agreement" section of Note 8 and "Corporate Borrowing Program – AEP System" section of Note 10.

Affiliated Revenues

AEGCo's revenues derived from sales to affiliates for the years ended December 31, 2018 and 2017 were $340 million and $341 million, respectively. These related party revenues are reported in Sales to AEP Affiliates on AEGCo's statements of income.

Unit Power Agreements (UPA)

Lawrenceburg UPA

OPCo and AEGCo entered into a 10-year UPA for the entire output from the Lawrenceburg Generating Station effective with AEGCo's purchase of the plant in May 2007. AEGCo's gross investment in the plant was $762 million as of December 31, 2016, net depreciation of $452 million. The Lawrenceburg UPA was assigned by OPCo to AGR. AGR had an option to extend the UPA for an additional two years. I&M operated the plant under an agreement with AEGCo. Under the UPA, AGR paid AEGCo for the capacity, depreciation, fuel, operation and maintenance and tax expenses. These payments were due regardless of whether the plant was operating. The fuel and operation and maintenance payments were based on actual costs incurred. All expenses were trued up periodically. The revenues from this agreement are included in Affiliated Revenues discussed above. This agreement terminated upon completion of the sale of the Lawrenceburg Generating Station in January 2017.

UPA between AEGCo and I&M

A UPA between AEGCo and I&M (the I&M Power Agreement) provides for the sale by AEGCo to I&M of all the power (and the energy associated therewith) available to AEGCo at the Rockport Plant unless it is sold to another utility. Subsequently, I&M assigns 30% of the power to KPCo. See the "UPA between AEGCo and KPCo" section below. I&M is obligated, whether or not power is available from AEGCo, to pay as a demand charge for the right to receive such power (and as an energy charge for any associated energy taken by I&M) net of amounts received by AEGCo from any other sources, sufficient to enable AEGCo to pay all its operating and other expenses, including a rate of return on the common equity of AEGCo as approved by the FERC. The revenues from this agreement are included in Affiliated Revenues discussed above. The I&M Power Agreement will continue in effect until the expiration of the lease term of Unit 2 of the Rockport Plant unless extended in specified circumstances.

UPA between AEGCo and KPCo

Pursuant to an assignment between I&M and KPCo and a UPA between AEGCo and KPCo, AEGCo sells KPCo 30% of the power (and the energy associated therewith) available to AEGCo from both units of the Rockport Plant. KPCo pays to AEGCo in consideration for the right to receive such power the same amounts which I&M would have paid AEGCo under the terms of the I&M Power Agreement for such entitlement. The revenues from this agreement are included in Affiliated Revenues discussed above. The KPCo UPA ends in December 2022.

Cook Coal Terminal

Cook Coal Terminal performs coal transloading and storage services at cost for I&M. AEGCo recorded revenues of $12.4 million and $10.2 million for the years ended December 31, 2018 and 2017, respectively, for transloading services provided. AEGCo included revenues for these services in Other Revenues - Affiliated on the statements of income.

Cook Coal Terminal also performs railcar maintenance services at cost for I&M, PSO and SWEPCo. AEGCo recorded revenues of $5.7 million and $5.3 million for the years ended December 31, 2018 and 2017, respectively, for railcar maintenance provided. AEGCo included revenues for these services in Other Revenues - Affiliated on the statements of income.

I&M Barging and Other Services

I&M provides barging and other transportation services to affiliates. AEGCo recorded expenses of $19.9 million and $15.3 million for the years ended December 31, 2018 and 2017, respectively, for barging services provided by I&M. These expenses were recorded in Fuel and Other Consumables Used for Electric Generation on AEGCo's statements of income.

Sales and Purchases of Property

AEGCo had affiliated sales and purchases of electric property individually amounting to $100 thousand or more. There were no gains or losses recorded on the transactions. The following table shows the sales and purchases, recorded at net book value, for the years ended December 31, 2018 and 2017:

	Years Ended December 31,	
	2018	**2017**
	(in thousands)	
Sales	$ 75	$ —
Purchases	—	—

The amounts above are recorded in Property, Plant and Equipment on the balance sheets.

12. VARIABLE INTEREST ENTITIES

The accounting guidance for "Variable Interest Entities" is a consolidation model that considers if a company has a variable interest in a VIE. A VIE is a legal entity that possesses any of the following conditions: the entity's equity at risk is not sufficient to permit the legal entity to finance its activities without additional subordinated financial support, equity owners are unable to direct the activities that most significantly impact the legal entity's economic performance (or they possess disproportionate voting rights in relation to the economic interest in the legal entity), or the equity owners lack the obligation to absorb the legal entity's expected losses or the right to receive the legal entity's expected residual returns. Entities are required to consolidate a VIE when it is determined that they have a controlling financial interest in a VIE and therefore, are the primary beneficiary of that VIE, as defined by the accounting guidance for "Variable Interest Entities." In determining whether AEGCo is the primary beneficiary of a VIE, management considers whether AEGCo has the power to direct the most significant activities of the VIE and is obligated to absorb losses or receive the expected residual returns that are significant to the VIE. Management believes that significant assumptions and judgments were applied consistently. AEGCo is not the primary beneficiary of any VIE and has not provided financial or other support to any VIE that was not previously contractually required.

AEPSC provides certain managerial and professional services to AEP's subsidiaries. Parent is the sole equity owner of AEPSC. AEP management controls the activities of AEPSC. The costs of the services are based on a direct charge or on a prorated basis and billed to the AEP subsidiary companies at AEPSC's cost. AEP subsidiaries have not provided financial or other support outside the reimbursement of costs for services rendered. AEPSC finances its operations through cost reimbursement from other AEP subsidiaries. There are no other terms or arrangements between AEPSC and any of the AEP subsidiaries that could require additional financial support from an AEP subsidiary or expose them to losses outside of the normal course of business. AEPSC and its billings are subject to regulation by the FERC. AEP subsidiaries are exposed to losses to the extent they cannot recover the costs of AEPSC through their normal business operations. AEP subsidiaries are considered to have a significant interest in AEPSC due to their activity in AEPSC's cost reimbursement structure. However, AEP subsidiaries do not have control over AEPSC. AEPSC is consolidated by AEP. In the event AEPSC would require financing or other support outside the cost reimbursement billings, this financing would be provided by AEP. AEGCo's total billings from AEPSC for the years ended December 31, 2018 and 2017 were $1.7 million and $2 million, respectively. The carrying amount of liabilities associated with AEPSC as of December 31, 2018 and 2017 was $161 thousand and $150 thousand, respectively. Management estimates the maximum exposure of loss to be equal to the amount of such liability.

13. PROPERTY, PLANT AND EQUIPMENT

Property, Plant and Equipment is shown functionally on the face of AEGCo's balance sheets. The following table includes AEGCo's total plant balances as of December 31, 2018 and 2017:

	December 31, 2018	December 31, 2017
	(in thousands)	
Regulated Property, Plant and Equipment		
Generation	$ 1,125,208	$ 1,111,563
Other	35,435	35,186
CWIP	50,525	27,721
Less: Accumulated Depreciation	719,639	677,587
Total Regulated Property, Plant and Equipment - Net	491,529	496,883
Nonregulated Property, Plant and Equipment - Net	84	130
Total Property, Plant and Equipment - Net	$ 491,613	$ 497,013

Depreciation

AEGCo provides for depreciation of Property, Plant and Equipment on a straight-line basis over the estimated useful lives of property, generally using composite rates by functional class. The following table provides total regulated annual composite depreciation rates and depreciable lives for AEGCo. Nonregulated depreciation rate ranges and depreciable life ranges are not applicable or not meaningful (NM) for 2018 and 2017.

	2018		2017	
Functional Class of Property	Annual Composite Depreciation Rate	Depreciable Life Ranges	Annual Composite Depreciation Rate	Depreciable Life Ranges
		(in years)		(in years)
Generation	4.0%	60	3.7%	60
Other	9.8%	NM	9.2%	NM

The composite depreciation rate generally includes a component for non-asset retirement obligation (non-ARO) removal costs, which is credited to Accumulated Depreciation and Amortization on the balance sheets. Actual removal costs incurred are charged to Accumulated Depreciation and Amortization. Any excess of accrued non-ARO removal costs over actual removal costs incurred is reclassified from Accumulated Depreciation and Amortization and reflected as a regulatory liability.

Asset Retirement Obligations (ARO)

AEGCo records ARO in accordance with the accounting guidance for "Asset Retirement and Environmental Obligations" for the retirement of ash disposal facilities and asbestos removal.

The following is a reconciliation of the 2018 and 2017 aggregate carrying amounts of ARO for AEGCo:

Year	ARO as of January 1,	Accretion Expense	Liabilities Incurred	Liabilities Settled	Revisions in Cash Flow Estimates	ARO as of December 31,
			(in thousands)			
2018	$ 17,072	$ 767	$ —	$ (32)	$ 1,070	$ 18,877
2017	8,550	608	22	(3)	7,895 (a)	17,072

(a) Revision is related to the timing of cash flows due to a change in the expected retirement date for Rockport Plant, Unit 1 from 2044 to 2028.

Allowance for Funds Used During Construction

AEGCo's amounts of allowance for equity and borrowed funds used during construction are summarized in the following table:

	Years Ended December 31, 2018	2017
	(in thousands)	
Allowance for Equity Funds Used During Construction	$ 844	$ 3,060
Allowance for Borrowed Funds Used During Construction	275	937

Jointly-owned Electric Facilities

AEGCo, jointly with I&M, owns one generating unit (Unit 1) of the Rockport Plant. AEGCo and I&M each have a 50% ownership share of the Rockport Plant. Using its own financing, each participating company is obligated to pay its share of the costs in the same proportion as its ownership interest. AEGCo's proportionate share of the operating costs associated with this facility is included in its statements of income and the investment and accumulated depreciation are reflected in its balance sheets under Property, Plant and Equipment as follows:

	Fuel	Percent of Ownership	Utility Plant in Service	Construction Work In Progress	Accumulated Depreciation
				(in thousands)	
AEGCo's Share as of December 31, 2018					
Rockport Generating Plant (a)(b)	Coal	50.0%	$ 1,098,865	$ 50,340	$ 726,039
AEGCo's Share as of December 31, 2017					
Rockport Generating Plant (a)(b)	Coal	50.0%	$ 1,084,622	$ 27,535	$ 687,286

(a) Operated by I&M.

(b) Amounts include AEGCo's 50% ownership of both Unit 1 and capital additions for Unit 2. Unit 2 is subject to an operating lease with a non-affiliated company. See the "Rockport Lease" section of Note 9.

14. 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 the year ended December 31, 2018.

Performance Obligations

AEGCo has performance obligations as part of its normal course of business. A performance obligation is a promise to transfer a distinct good or service, or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to a customer. The invoice practical expedient within the accounting guidance for "Revenue from Contracts with Customers" allows for the recognition of revenue from performance obligations in the amount of consideration to which there is a right to invoice the customer and when the amount for which there is a right to invoice corresponds directly to the value transferred to the customer.

The purpose of the invoice practical expedient is to depict an entity's measure of progress toward completion of the performance obligation within a contract and can only be applied to performance obligations that are satisfied over time and when the invoice is representative of services provided to date. AEGCo elected to apply the invoice practical expedient to recognize revenue for performance obligations satisfied over time as the invoices from the respective revenue streams are representative of services or goods provided to date to the customer. Performance obligations for AEGCo are summarized as follows:

Wholesale Revenues - Generation Affiliated

AEGCo engages in the generation and wholesale sale of electric power to its affiliates, I&M and KPCo. AEGCo derives operating revenues from the sale of Rockport Plant energy and capacity to I&M and KPCo pursuant to FERC-approved long-term UPAs. Under the UPAs, AEGCo has a performance obligation to supply wholesale generation electricity to I&M and KPCo.

The UPAs provide FERC-approved rate of return on common equity, a return on capital (net of temporary cash investments) and recovery of costs including operation and maintenance, fuel and taxes. Under the terms of the UPAs, AEGCo accumulates all expenses monthly and prepares bills for its affiliates. In the month the expenses are incurred, AEGCo recognizes the billing revenues and establishes a receivable from the affiliated companies. The costs of operating the plants are billed to the affiliates receiving the benefits under the UPAs on a monthly basis. AEGCo's performance obligations under the UPAs are satisfied over time as I&M and KPCo simultaneously receive and consume the wholesale electricity.

Fixed Performance Obligations

As of December 31, 2018, 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 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 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 were not material as of December 31, 2018.

Contract Costs

Contract costs to obtain or fulfill a contract are accounted for under the guidance for "Other Assets and Deferred Costs" and presented as a single asset and neither bifurcated nor reclassified between current and noncurrent assets on AEGCo's balance sheets. Contract costs to acquire a contract are amortized in a manner consistent with the transfer of goods or services to the customer in Other Operation on AEGCo's statements of income. AEGCo did not have material contract costs as of December 31, 2018.