Kentucky Power Company

2021 Third Quarter Report

Financial Statements

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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
AEP	American Electric Power Company, Inc., an investor-owned electric public utility holding company which includes American Electric Power Company, Inc. (Parent) and majority owned consolidated subsidiaries and consolidated affiliates.
AEP Credit	AEP Credit, Inc., a consolidated variable interest entity of AEP which securitizes accounts receivable and accrued utility revenues for affiliated electric utility companies.
AEP System	American Electric Power System, an electric system, owned and operated by AEP subsidiaries.
AEPSC	American Electric Power Service Corporation, an AEP service subsidiary providing management and professional services to AEP and its subsidiaries.
AFUDC	Allowance for Equity Funds Used During Construction.
AOCI	Accumulated Other Comprehensive Income.
APCo	Appalachian Power Company, an AEP electric utility subsidiary.
ASU	Accounting Standards Update.
CCR	Coal Combustion Residual.
COVID-19	Coronavirus 2019, a highly infectious respiratory disease. In March 2020, the World Health Organization declared COVID-19 a worldwide pandemic.
CWIP	Construction Work in Progress.
ELG	Effluent Limitation Guidelines.
Excess ADIT	Excess accumulated deferred income taxes.
FASB	Financial Accounting Standards Board.
FERC	Federal Energy Regulatory Commission.
FTR	Financial Transmission Right, a financial instrument that entitles the holder to receive compensation for certain congestion-related transmission charges that arise when the power grid is congested resulting in differences in locational prices.
GAAP	Accounting Principles Generally Accepted in the United States of America.
I&M	Indiana Michigan Power Company, an AEP electric utility subsidiary.
IRS	Internal Revenue Service.
KPCo	Kentucky Power Company, an AEP electric utility subsidiary.
KPSC	Kentucky Public Service Commission.
MTM	Mark-to-Market.
MWh	Megawatt-hour.
OPEB	Other Postretirement Benefits.
OTC	Over-the-counter.
Parent	American Electric Power Company, Inc., the equity owner of AEP subsidiaries within the AEP consolidation.
PJM	Pennsylvania – New Jersey – Maryland regional transmission organization.
Risk Management Contracts	Trading and non-trading derivatives, including those derivatives designated as cash flow and fair value hedges.
Tax Reform	On December 22, 2017, President Trump signed into law legislation referred to as the "Tax Cuts and Jobs Act" (the TCJA). The TCJA includes significant changes to the Internal Revenue Code of 1986, including a reduction in the corporate federal income tax rate from 35% to 21% effective January 1, 2018.
Utility Money Pool	Centralized funding mechanism AEP uses to meet the short-term cash requirements of certain utility subsidiaries.
WPCo	Wheeling Power Company, an AEP electric utility subsidiary.
WVPSC	Public Service Commission of West Virginia.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF INCOME
For the Three and Nine Months Ended September 30, 2021 and 2020
(in thousands)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	**2020**	**2021**	**2020**
REVENUES				
Electric Generation, Transmission and Distribution	$ 163,133	$ 134,616	$ 469,081	$ 398,095
Sales to AEP Affiliates	2,658	2,747	7,885	9,265
Other Revenues	252	189	754	601
TOTAL REVENUES	166,043	137,552	477,720	407,961
EXPENSES				
Fuel and Other Consumables Used for Electric Generation	31,919	20,172	72,510	60,677
Purchased Electricity for Resale	7,406	6,261	39,305	23,326
Purchased Electricity from AEP Affiliates	27,112	23,941	73,985	58,182
Other Operation	31,295	25,360	91,585	68,621
Maintenance	15,905	13,180	51,207	53,196
Depreciation and Amortization	28,502	25,262	85,154	74,714
Taxes Other Than Income Taxes	6,984	7,028	20,999	21,049
TOTAL EXPENSES	149,123	121,204	434,745	359,765
OPERATING INCOME	16,920	16,348	42,975	48,196
Other Income (Expense):				
Other Income	535	202	1,218	831
Non-Service Cost Components of Net Periodic Benefit Cost	1,035	1,014	3,106	3,042
Interest Expense	(8,845)	(9,363)	(26,701)	(28,801)
INCOME BEFORE INCOME TAX BENEFIT	9,645	8,201	20,598	23,268
Income Tax Benefit	(11,038)	(1,880)	(24,233)	(4,713)
NET INCOME	$ 20,683	$ 10,081	$ 44,831	$ 27,981

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

See Condensed Notes to Condensed Financial Statements beginning on page 8.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
For the Three and Nine Months Ended September 30, 2021 and 2020
(in thousands)
(Unaudited)

	Three Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
Net Income	$ 20,683	$ 10,081	$ 44,831	$ 27,981
OTHER COMPREHENSIVE LOSS, NET OF TAXES				
Amortization of Pension and OPEB Deferred Costs, Net of Tax of $(9) and $(7) for the Three Months Ended September 30, 2021 and 2020, Respectively, and $(27) and $(21) for the Nine Months Ended September 30, 2021 and 2020, Respectively	(34)	(27)	(102)	(80)
TOTAL COMPREHENSIVE INCOME	$ 20,649	$ 10,054	$ 44,729	$ 27,901

See Condensed Notes to Condensed Financial Statements beginning on page 8.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF CHANGES IN
COMMON SHAREHOLDER'S EQUITY
For the Nine Months Ended September 30, 2021 and 2020
(in thousands)
(Unaudited)

	Common Stock	Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
TOTAL COMMON SHAREHOLDER'S EQUITY - DECEMBER 31, 2019	$ 50,450	$ 526,135	$ 204,806	$ 790	$ 782,181
ASU 2016-13 Adoption			48		48
Net Income			18,835		18,835
Other Comprehensive Loss				(27)	(27)
TOTAL COMMON SHAREHOLDER'S EQUITY - MARCH 31, 2020	50,450	526,135	223,689	763	801,037
Net Loss			(935)		(935)
Other Comprehensive Loss				(26)	(26)
TOTAL COMMON SHAREHOLDER'S EQUITY - JUNE 30, 2020	50,450	526,135	222,754	737	800,076
Net Income			10,081		10,081
Other Comprehensive Loss				(27)	(27)
TOTAL COMMON SHAREHOLDER'S EQUITY - SEPTEMBER 30, 2020	$ 50,450	$ 526,135	$ 232,835	$ 710	$ 810,130
TOTAL COMMON SHAREHOLDER'S EQUITY - DECEMBER 31, 2020	$ 50,450	$ 526,135	$ 245,871	$ 878	$ 823,334
Net Income			13,851		13,851
Other Comprehensive Loss				(34)	(34)
TOTAL COMMON SHAREHOLDER'S EQUITY - MARCH 31, 2021	50,450	526,135	259,722	844	837,151
Net Income			10,297		10,297
Other Comprehensive Loss				(34)	(34)
TOTAL COMMON SHAREHOLDER'S EQUITY - JUNE 30, 2021	50,450	526,135	270,019	810	847,414
Net Income			20,683		20,683
Other Comprehensive Loss				(34)	(34)
TOTAL COMMON SHAREHOLDER'S EQUITY - SEPTEMBER 30, 2021	$ 50,450	$ 526,135	$ 290,702	$ 776	$ 868,063

See Condensed Notes to Condensed Financial Statements beginning on page 8.

KENTUCKY POWER COMPANY
CONDENSED BALANCE SHEETS
ASSETS
September 30, 2021 and December 31, 2020
(in thousands)
(Unaudited)

	September 30, 2021	December 31, 2020
CURRENT ASSETS		
Cash and Cash Equivalents	$ 1,155	$ 1,533
Accounts Receivable:		
Customers	7,819	10,485
Affiliated Companies	21,071	21,019
Accrued Unbilled Revenues	16,508	18,918
Miscellaneous	111	80
Allowance for Uncollectible Accounts	(11)	(87)
Total Accounts Receivable	45,498	50,415
Fuel	7,696	22,487
Materials and Supplies	18,853	19,861
Risk Management Assets	5,758	3,152
Accrued Tax Benefits	12,313	468
Regulatory Asset for Under-Recovered Fuel Costs	5,740	—
Prepayments and Other Current Assets	5,728	3,034
TOTAL CURRENT ASSETS	102,741	100,950
PROPERTY, PLANT AND EQUIPMENT		
Electric:		
Generation	1,229,655	1,231,387
Transmission	720,112	703,309
Distribution	985,257	955,501
Other Property, Plant and Equipment	133,205	120,965
Construction Work in Progress	126,312	83,008
Total Property, Plant and Equipment	3,194,541	3,094,170
Accumulated Depreciation and Amortization	1,094,426	1,052,273
TOTAL PROPERTY, PLANT AND EQUIPMENT – NET	2,100,115	2,041,897
OTHER NONCURRENT ASSETS		
Regulatory Assets	495,946	450,145
Long-term Risk Management Assets	—	23
Employee Benefits and Pension Assets	42,831	41,062
Operating Lease Assets	10,954	11,928
Deferred Charges and Other Noncurrent Assets	19,904	33,585
TOTAL OTHER NONCURRENT ASSETS	569,635	536,743
TOTAL ASSETS	$ 2,772,491	$ 2,679,590

See Condensed Notes to Condensed Financial Statements beginning on page 8.

KENTUCKY POWER COMPANY
CONDENSED BALANCE SHEETS
LIABILITIES AND COMMON SHAREHOLDER'S EQUITY
September 30, 2021 and December 31, 2020
(Unaudited)

	September 30, 2021	December 31, 2020
	(in thousands)	
CURRENT LIABILITIES		
Advances from Affiliates	$ 13,811	$ 65,647
Accounts Payable:		
General	50,158	47,157
Affiliated Companies	27,219	24,862
Long-term Debt Due Within One Year – Nonaffiliated	125,000	40,000
Risk Management Liabilities	268	213
Customer Deposits	31,876	30,774
Accrued Taxes	24,122	36,191
Accrued Interest	5,906	6,399
Obligations Under Operating Leases	2,191	2,296
Regulatory Liability for Over-Recovered Fuel Costs	—	313
Other Current Liabilities	27,623	26,767
TOTAL CURRENT LIABILITIES	308,174	280,619
NONCURRENT LIABILITIES		
Long-term Debt – Nonaffiliated	977,989	952,650
Long-term Risk Management Liabilities	—	19
Deferred Income Taxes	440,899	446,054
Regulatory Liabilities and Deferred Investment Tax Credits	139,067	133,243
Asset Retirement Obligations	17,868	21,544
Employee Benefits and Pension Obligations	7,527	7,970
Obligations Under Operating Leases	8,802	9,672
Deferred Credits and Other Noncurrent Liabilities	4,102	4,485
TOTAL NONCURRENT LIABILITIES	1,596,254	1,575,637
TOTAL LIABILITIES	1,904,428	1,856,256
Rate Matters (Note 4)		
Commitments and Contingencies (Note 5)		
COMMON SHAREHOLDER'S EQUITY		
Common Stock – Par Value – $50 Per Share:		
Authorized – 2,000,000 Shares		
Outstanding – 1,009,000 Shares	50,450	50,450
Paid-in Capital	526,135	526,135
Retained Earnings	290,702	245,871
Accumulated Other Comprehensive Income (Loss)	776	878
TOTAL COMMON SHAREHOLDER'S EQUITY	868,063	823,334
TOTAL LIABILITIES AND COMMON SHAREHOLDER'S EQUITY	$ 2,772,491	$ 2,679,590

See Condensed Notes to Condensed Financial Statements beginning on page 8.

KENTUCKY POWER COMPANY
CONDENSED STATEMENTS OF CASH FLOWS
For the Nine Months Ended September 30, 2021 and 2020
(in thousands)
(Unaudited)

	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
OPERATING ACTIVITIES		
Net Income	$ 44,831	$ 27,981
Adjustments to Reconcile Net Income to Net Cash Flows from Operating Activities:		
Depreciation and Amortization	85,154	74,714
Deferred Income Taxes	(13,538)	550
Allowance for Equity Funds Used During Construction	(1,202)	(766)
Mark-to-Market of Risk Management Contracts	(2,547)	444
Pension Contributions to Qualified Plan Trust	—	(2,775)
Property Taxes	14,486	14,444
Deferred Fuel Over/Under-Recovery, Net	(6,053)	2,332
Change in Regulatory Assets	(53,243)	(27,952)
Change in Other Noncurrent Assets	(11,268)	(9,203)
Change in Other Noncurrent Liabilities	1,521	(9,204)
Changes in Certain Components of Working Capital:		
Accounts Receivable, Net	5,414	7,323
Fuel, Materials and Supplies	15,895	2,901
Accounts Payable	2,363	(3,759)
Accrued Taxes, Net	(23,914)	(12,931)
Other Current Assets	(2,702)	(1,332)
Other Current Liabilities	1,461	(2,856)
Net Cash Flows from Operating Activities	56,658	59,911
INVESTING ACTIVITIES		
Construction Expenditures	(117,816)	(121,934)
Other Investing Activities	3,173	1,116
Net Cash Flows Used for Investing Activities	(114,643)	(120,818)
FINANCING ACTIVITIES		
Issuance of Long-term Debt – Nonaffiliated	149,974	124,619
Change in Advances from Affiliates, Net	(51,836)	(63,233)
Retirement of Long-term Debt – Nonaffiliated	(40,000)	—
Principal Payments for Finance Lease Obligations	(693)	(607)
Other Financing Activities	162	132
Net Cash Flows from Financing Activities	57,607	60,911
Net Increase (Decrease) in Cash and Cash Equivalents	(378)	4
Cash and Cash Equivalents at Beginning of Period	1,533	849
Cash and Cash Equivalents at End of Period	$ 1,155	$ 853
SUPPLEMENTARY INFORMATION		
Cash Paid for Interest, Net of Capitalized Amounts	$ 28,181	$ 28,753
Net Cash Paid (Received) for Income Taxes	1,991	(5,835)
Noncash Acquisitions Under Finance Leases	288	690
Construction Expenditures Included in Current Liabilities as of September 30,	21,049	17,201

See Condensed Notes to Condensed Financial Statements beginning on page 8.

INDEX OF CONDENSED NOTES TO CONDENSED FINANCIAL STATEMENTS

1. SIGNIFICANT ACCOUNTING MATTERS

General

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

In the opinion of management, the unaudited condensed interim financial statements reflect all normal and recurring accruals and adjustments necessary for a fair statement of the net income, financial position and cash flows for the interim periods. Net income for the three and nine months ended September 30, 2021 is not necessarily indicative of results that may be expected for the year ending December 31, 2021. The condensed financial statements are unaudited and should be read in conjunction with the audited 2020 financial statements and notes thereto, which are included in KPCo's 2020 Annual Report.

Subsequent Events

Management reviewed subsequent events through October 28, 2021, the date that the third quarter 2021 report was available to be issued.

2. NEW ACCOUNTING STANDARDS

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

3. COMPREHENSIVE INCOME

Presentation of Comprehensive Income

The following tables provide the components of changes in AOCI and details of reclassifications from AOCI. The amortization of pension and OPEB AOCI components are included in the computation of net periodic pension and OPEB costs. See Note 6 - Benefit Plans for additional information.

Three Months Ended September 30, 2021	**Pension and OPEB (in thousands)**
Balance in AOCI as of June 30, 2021	$ 810
Change in Fair Value Recognized in AOCI	—
Amount of (Gain) Loss Reclassified from AOCI	
Amortization of Prior Service Cost (Credit)	(59)
Amortization of Actuarial (Gains) Losses	16
Reclassifications from AOCI, before Income Tax (Expense) Benefit	(43)
Income Tax (Expense) Benefit	(9)
Reclassifications from AOCI, Net of Income Tax (Expense) Benefit	(34)
Net Current Period Other Comprehensive Income (Loss)	(34)
Balance in AOCI as of September 30, 2021	$ 776

Three Months Ended September 30, 2020	**Pension and OPEB (in thousands)**
Balance in AOCI as of June 30, 2020	$ 737
Change in Fair Value Recognized in AOCI	—
Amount of (Gain) Loss Reclassified from AOCI	
Amortization of Prior Service Cost (Credit)	(57)
Amortization of Actuarial (Gains) Losses	23
Reclassifications from AOCI, before Income Tax (Expense) Benefit	(34)
Income Tax (Expense) Benefit	(7)
Reclassifications from AOCI, Net of Income Tax (Expense) Benefit	(27)
Net Current Period Other Comprehensive Income (Loss)	(27)
Balance in AOCI as of September 30, 2020	$ 710

Nine Months Ended September 30, 2021	Pension and OPEB
	(in thousands)
Balance in AOCI as of December 31, 2020	$ 878
Change in Fair Value Recognized in AOCI	—
Amount of (Gain) Loss Reclassified from AOCI	
Amortization of Prior Service Cost (Credit)	(176)
Amortization of Actuarial (Gains) Losses	47
Reclassifications from AOCI, before Income Tax (Expense) Benefit	(129)
Income Tax (Expense) Benefit	(27)
Reclassifications from AOCI, Net of Income Tax (Expense) Benefit	(102)
Net Current Period Other Comprehensive Income (Loss)	(102)
Balance in AOCI as of September 30, 2021	$ 776

Nine Months Ended September 30, 2020	Pension and OPEB
	(in thousands)
Balance in AOCI as of December 31, 2019	$ 790
Change in Fair Value Recognized in AOCI	—
Amount of (Gain) Loss Reclassified from AOCI	
Amortization of Prior Service Cost (Credit)	(171)
Amortization of Actuarial (Gains) Losses	70
Reclassifications from AOCI, before Income Tax (Expense) Benefit	(101)
Income Tax (Expense) Benefit	(21)
Reclassifications from AOCI, Net of Income Tax (Expense) Benefit	(80)
Net Current Period Other Comprehensive Income (Loss)	(80)
Balance in AOCI as of September 30, 2020	$ 710

4. RATE MATTERS

As discussed in KPCo's 2020 Annual Report, KPCo is involved in rate and regulatory proceedings at the FERC and the KPSC. The Rate Matters note within KPCo's 2020 Annual Report should be read in conjunction with this report to gain a complete understanding of material rate matters still pending that could impact net income, cash flows and possibly financial condition. The following discusses ratemaking developments in 2021 and updates KPCo's 2020 Annual Report.

Regulatory Assets Pending Final Regulatory Approval

Noncurrent Regulatory Assets	September 30, 2021	December 31, 2020
	(in thousands)	
Regulatory Assets Currently Earning a Return		
Kentucky Deferred Purchased Power Expenses	$ 45,949	$ 41,267
Regulatory Assets Currently Not Earning a Return		
Storm-Related Costs	53,092	10,708
Other Regulatory Assets Pending Final Regulatory Approval	724	2,065
Total Regulatory Assets Pending Final Regulatory Approval	$ 99,765	$ 54,040

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

Storm-Related Costs

In December 2020, a snow storm impacted KPCo's service territory resulting in customer outages and damage to KPCo utility assets. In March 2021, KPCo filed an application seeking deferral authority of approximately $1 million related to the December 2020 storm.

In February 2021, a severe winter storm impacted KPCo's service territory resulting in customer outages and extensive damage to transmission and distribution infrastructure. Management currently estimates KPCo incurred incremental operations and maintenance expenses of $47.6 million related to the storm, of which $42.6 million has been deferred as a regulatory asset. Incremental capital expenditures are estimated to be $29 million.

In April, 2021 the KPSC approved KPCo's requests for deferral authority of the December 2020 and February 2021 storm-related costs. KPCo will seek recovery of the deferred storm costs in its next base rate case.

If any of these incremental storm costs are not recoverable, it could reduce future net income and cash flows and impact financial condition.

CCR/ELG Compliance Plan Filings

KPCo and WPCo each own a 50% interest in the Mitchell Plant. In December 2020 and February 2021, WPCo and KPCo filed requests with the WVPSC and KPSC, respectively, to obtain the regulatory approvals necessary to implement CCR and ELG compliance plans and seek recovery of the estimated $132 million investment for the Mitchell Plant that would allow the plant to continue operating beyond 2028. Within those requests, WPCo and KPCo also filed a $25 million alternative to implement only the CCR-related investments with the WVPSC and KPSC, respectively, which would allow the Mitchell Plant to continue operating only through 2028.

In July 2021, the KPSC issued an order approving the CCR only alternative and rejecting the full CCR and ELG compliance plan. In August 2021, the WVPSC approved the full CCR and ELG compliance plan for the WPCo share of the Mitchell Plant. In September 2021, WPCo submitted a filing with the WVPSC to reopen the CCR/ELG case that was approved by the WVPSC in August 2021. Due to the rejection by the KPSC of the KPCo share of the ELG investments, WPCo requested the WVPSC consider approving the construction and recovery of all ELG costs at the plant. In October 2021, the WVPSC affirmed its August 2021 order approving the construction of CCR/ELG investments and directed WPCo to proceed with CCR/ELG compliance plans that would allow the plant to continue operating beyond 2028. The WVPSC's order further states WPCo will not share capacity and energy from the plant with KPCo customers if those customers are not paying for ELG compliance costs, or for any new capital investment or continuing operations costs incurred, to allow the plant to operate beyond 2028 or prevent downgrades prior to 2028. The WVPSC also ordered that WPCo will be given the opportunity to recover, from its customers, the new capital and operating costs arising solely from the WVPSC's directive to operate the plant beyond 2028 if the WVPSC finds that the costs are reasonably and prudently incurred. In October 2021, an intervenor filed a petition for reconsideration at the WVPSC requesting clarification on certain aspects of the order, primarily the jurisdictional allocation of future operating expenses and plant costs.

As of September 30, 2021, KPCo's share of the Mitchell Plant's ELG investment balance in CWIP was $1.7 million. As of September 30, 2021, the net book value of KPCo's share of the Mitchell Plant, before cost of removal including CWIP and inventory, was $586.5 million.

If any of the ELG costs are not approved for recovery and/or the retirement date of the Mitchell Plant is accelerated to 2028 without commensurate cost recovery, it would reduce future net income and cash flows and impact financial condition.

Strategic Evaluation KPSC Hearings

In September 2021, the KPSC initiated a proceeding to investigate the service, rates and facilities of KPCo. An initial hearing was held in early October 2021 and KPCo's testimony addressed the following topics, as ordered by the KPSC: (a) how AEP's strategic evaluation of the Kentucky assets has impacted KPCo's operations, service, financial, planning and business decisions, including those related to distribution, transmission and generation function, (b) what actions KPCo has taken as a result of the announced strategic evaluation, (c) what decisions KPCo has made that it otherwise would not have absent a strategic evaluation, (d) which documents will be implicated should the strategic evaluation result in AEP's divestment of KPCo, and how those documents will affect KPCo and their customers (which documents may include, but are not limited to the Mitchell Operating Agreement, AEP East Transmission Owners' Agreement filed with the FERC, and any PJM governing documents) and (e) the follow-on impact to KPCo and its customers should it become its own PJM zone, including the interaction with the PJM base residual auction.

5. COMMITMENTS, GUARANTEES AND CONTINGENCIES

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

For current proceedings not specifically discussed below, management does not anticipate that the liabilities, if any, arising from such proceedings would have a material effect on the financial statements. The Commitments, Guarantees and Contingencies note within KPCo's 2020 Annual Report should be read in conjunction with this report.

GUARANTEES

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

Indemnifications and Other Guarantees

Contracts

KPCo enters into certain types of contracts which require indemnifications. Typically these contracts include, but are not limited to, sale agreements, lease agreements, purchase agreements and financing agreements. Generally, these agreements may include, but are not limited to, indemnifications around certain tax, contractual and environmental matters. With respect to sale agreements, exposure generally does not exceed the sale price. As of September 30, 2021, there were no material liabilities recorded for any indemnifications.

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

Master Lease Agreements

KPCo leases certain equipment under master lease agreements. Under the lease agreements, the lessor is guaranteed a residual value up to a stated percentage of the equipment cost at the end of the lease term. If the actual fair value of the leased equipment is below the guaranteed residual value at the end of the lease term, KPCo is committed to pay the difference between the actual fair value and the residual value guarantee. Historically, at the end of the lease term the fair value has been in excess of the amount guaranteed. As of September 30, 2021, the maximum potential loss for these lease agreements was $1.7 million assuming the fair value of the equipment is zero at the end of the lease term.

CONTINGENCIES

Claims Challenging Transition of American Electric Power System Retirement Plan to Cash Balance Formula

The American Electric Power System Retirement Plan (the Plan) has received a letter written on behalf of four participants (the Claimants) making a claim for additional plan benefits and purporting to advance such claims on behalf of a class. When the Plan's benefit formula was changed in the year 2000, AEP provided a special provision for employees hired before January 1, 2001, allowing them to continue benefit accruals under the then benefit formula for a full 10 years alongside of the new cash balance benefit formula then being implemented. Employees who were hired on or after January 1, 2001 accrued benefits only under the new cash balance benefit formula. The Claimants have asserted claims that: (a) the Plan violates the requirements under the Employee Retirement Income Security Act (ERISA) intended to preclude back-loading the accrual of benefits to the end of a participant's career, (b) the Plan violates the age discrimination prohibitions of ERISA and the Age Discrimination in Employment Act and (c) the company failed to provide required notice regarding the changes to the Plan. AEP has responded to the Claimants providing a reasoned explanation for why each of their claims have been denied. The denial of those claims was appealed to the AEP System Retirement Plan Appeal Committee and the Committee upheld the denial of claims. Management will continue to defend against the claims. Management is unable to determine a range of potential losses that is reasonably possible of occurring.

6. BENEFIT PLANS

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

Components of Net Periodic Benefit Cost

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

	Pension Plans		OPEB	
	Three Months Ended September 30,		Three Months Ended September 30,	
	2021	2020	2021	2020
	(in thousands)			
Service Cost	$ 869	$ 780	$ 71	$ 75
Interest Cost	1,210	1,493	274	373
Expected Return on Plan Assets	(2,145)	(2,473)	(869)	(941)
Amortization of Prior Service Credit	—	—	(625)	(613)
Amortization of Net Actuarial Loss	880	823	—	60
Net Periodic Benefit Cost (Credit)	$ 814	$ 623	$ (1,149)	$ (1,046)

	Pension Plans		OPEB	
	Nine Months Ended September 30,		Nine Months Ended September 30,	
	2021	2020	2021	2020
	(in thousands)			
Service Cost	$ 2,608	$ 2,339	$ 212	$ 224
Interest Cost	3,630	4,478	822	1,120
Expected Return on Plan Assets	(6,436)	(7,418)	(2,609)	(2,822)
Amortization of Prior Service Credit	—	—	(1,874)	(1,839)
Amortization of Net Actuarial Loss	2,641	2,469	—	179
Net Periodic Benefit Cost (Credit)	$ 2,443	$ 1,868	$ (3,449)	$ (3,138)

Qualified Pension Contribution

For the qualified pension plan, discretionary contributions may be made to maintain the funded status of the plan. In the third quarter of 2020, KPCo made a $2.8 million discretionary contribution to the qualified pension plan.

7. DERIVATIVES AND HEDGING

OBJECTIVES FOR UTILIZATION OF DERIVATIVE INSTRUMENTS

AEPSC is agent for and transacts on behalf of KPCo.

KPCo is exposed to certain market risks as a major power producer and participant in the electricity, natural gas, coal and emission allowance markets. These risks include commodity price risk, interest rate risk and credit risk. These risks represent the risk of loss that may impact KPCo due to changes in the underlying market prices or rates. Management utilizes derivative instruments to manage these risks.

STRATEGIES FOR UTILIZATION OF DERIVATIVE INSTRUMENTS TO ACHIEVE OBJECTIVES

Risk Management Strategies

The strategy surrounding the use of derivative instruments primarily focuses on managing risk exposures, future cash flows and creating value utilizing both economic and formal hedging strategies. The risk management strategies also include the use of derivative instruments for trading purposes which focus on seizing market opportunities to create value driven by expected changes in the market prices of the commodities. To accomplish these objectives, KPCo primarily employs risk management contracts including physical and financial forward purchase-and-sale contracts and, to a lesser extent, OTC swaps and options. Not all risk management contracts meet the definition of a derivative under the accounting guidance for “Derivatives and Hedging.” Derivative risk management contracts elected normal under the normal purchases and normal sales scope exception are not subject to the requirements of this accounting guidance.

KPCo utilizes power, capacity, coal, natural gas, interest rate and, to a lesser extent, heating oil, gasoline and other commodity contracts to manage the risk associated with the energy business. KPCo utilizes interest rate derivative contracts in order to manage the interest rate exposure associated with its commodity portfolio. For disclosure purposes, such risks are grouped as “Commodity,” as these risks are related to energy risk management activities. KPCo may also utilize derivative contracts to manage interest rate risk associated with debt financing. For disclosure purposes, these risks are grouped as “Interest Rate.” The amount of risk taken is determined by the Commercial Operations and Finance groups in accordance with the established risk management policies as approved by the Finance Committee of the Board of Directors.

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

Primary Risk Exposure	September 30, 2021	December 31, 2020	Unit of Measure
	(in thousands)		
Commodity:			
Power	11,699	8,249	MWhs
Heating Oil and Gasoline	302	270	Gallons

Cash Flow Hedging Strategies

KPCo utilizes cash flow hedges on certain derivative transactions for the purchase and sale of power ("Commodity") in order to manage the variable price risk related to forecasted purchases and sales. Management monitors the potential impacts of commodity price changes and, where appropriate, enters into derivative transactions to protect profit margins for a portion of future electricity sales and purchases. KPCo does not hedge all commodity price risk.

KPCo may utilize a variety of interest rate derivative transactions in order to manage interest rate risk exposure. KPCo may also utilize interest rate derivative contracts to manage interest rate exposure related to future borrowings of fixed-rate debt. KPCo does not hedge all interest rate exposure.

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

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

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

According to the accounting guidance for "Derivatives and Hedging," KPCo reflects the fair values of derivative instruments subject to netting agreements with the same counterparty net of related cash collateral. For certain risk management contracts, KPCo is required to post or receive cash collateral based on third-party contractual agreements and risk profiles. For the September 30, 2021 and December 31, 2020 balance sheets, KPCo netted \$136 thousand and \$96 thousand, respectively, of cash collateral received from third-parties against short-term and long-term risk management assets and \$3.1 million and \$0, respectively, of cash collateral paid to third-parties against short-term and long-term risk management liabilities.

The following tables represent the gross fair value of KPCo's derivative activity on the balance sheets:

Fair Value of Derivative Instruments
September 30, 2021

Balance Sheet Location	Risk Management Contracts – Commodity (a)	Gross Amounts Offset in the Statement of Financial Position (b)	Net Amounts of Assets/Liabilities Presented in the Statement of Financial Position (c)
		(in thousands)	
Current Risk Management Assets	$ 15,259	$ (9,501)	$ 5,758
Long-term Risk Management Assets	43	(43)	—
Total Assets	15,302	(9,544)	5,758
Current Risk Management Liabilities	12,765	(12,497)	268
Long-term Risk Management Liabilities	33	(33)	—
Total Liabilities	12,798	(12,530)	268
Total MTM Derivative Contract Net Assets	$ 2,504	$ 2,986	$ 5,490

December 31, 2020

Balance Sheet Location	Risk Management Contracts – Commodity (a)	Gross Amounts Offset in the Statement of Financial Position (b)	Net Amounts of Assets/Liabilities Presented in the Statement of Financial Position (c)
		(in thousands)	
Current Risk Management Assets	$ 6,751	$ (3,599)	$ 3,152
Long-term Risk Management Assets	139	(116)	23
Total Assets	6,890	(3,715)	3,175
Current Risk Management Liabilities	3,746	(3,533)	213
Long-term Risk Management Liabilities	105	(86)	19
Total Liabilities	3,851	(3,619)	232
Total MTM Derivative Contract Net Assets (Liabilities)	$ 3,039	$ (96)	$ 2,943

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

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

Amount of Gain (Loss) Recognized on
Risk Management Contracts

Location of Gain (Loss)	Three Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
	(in thousands)			
Electric Generation, Transmission and Distribution Revenues	$ (12)	$ 148	$ (12)	$ 170
Purchased Electricity for Resale	35	40	72	84
Other Operation	28	(16)	59	(44)
Maintenance	35	(24)	82	(75)
Regulatory Assets (a)	(1,955)	127	(3,226)	407
Regulatory Liabilities (a)	2,555	3,394	4,944	6,727
Total Gain on Risk Management Contracts	$ 686	$ 3,669	$ 1,919	$ 7,269

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

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

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

For contracts that have not been designated as part of a hedging relationship, the accounting for changes in fair value depends on whether the derivative instrument is held for trading purposes. Unrealized and realized gains and losses on derivative instruments held for trading purposes are included in revenues on a net basis on KPCo's statements of income. Unrealized and realized gains and losses on derivative instruments not held for trading purposes are included in revenues or expenses on KPCo's statements of income depending on the relevant facts and circumstances. Certain derivatives that economically hedge future commodity risk are recorded in the same line item on the statements of income as that of the associated risk being hedged. However, unrealized and some realized gains and losses for both trading and non-trading derivative instruments are recorded as regulatory assets (for losses) or regulatory liabilities (for gains), in accordance with the accounting guidance for "Regulated Operations."

Accounting for Cash Flow Hedging Strategies

For cash flow hedges (i.e. hedging the exposure to variability in expected future cash flows that is attributable to a particular risk), KPCo initially reports the gain or loss on the derivative instrument as a component of Accumulated Other Comprehensive Income (Loss) on the balance sheets until the period the hedged item affects Net Income.

Realized gains and losses on derivative contracts for the purchase and sale of power designated as cash flow hedges are included in Total Revenues or Purchased Electricity for Resale on KPCo's statements of income, or in Regulatory Assets or Regulatory Liabilities on KPCo's balance sheets, depending on the specific nature of the risk being hedged. During the three and nine months ended September 30, 2021 and 2020, KPCo did not apply cash flow hedging to outstanding power derivatives.

KPCo reclassifies gains and losses on interest rate derivative hedges related to debt financings from Accumulated Other Comprehensive Income (Loss) on its balance sheets into Interest Expense on its statements of income in those periods in which hedged interest payments occur. During the three and nine months ended September 30, 2021 and 2020, KPCo did not apply cash flow hedging to outstanding interest rate derivatives.

There was no impact of cash flow hedges included in Accumulated Other Comprehensive Income (Loss) on KPCo's balance sheets as of September 30, 2021 and December 31, 2020.

The actual amounts that KPCo reclassifies from Accumulated Other Comprehensive Income (Loss) to Net Income can differ due to market price changes. As of September 30, 2021, KPCo is not hedging (with contracts subject to the accounting guidance for "Derivatives and Hedging") its exposure to variability in future cash flows related to forecasted transactions.

Credit Risk

Management mitigates credit risk in KPCo's wholesale marketing and trading activities by assessing the creditworthiness of potential counterparties before entering into transactions with them and continuing to evaluate their creditworthiness on an ongoing basis. Management uses credit agency ratings and current market-based qualitative and quantitative data as well as financial statements to assess the financial health of counterparties on an ongoing basis.

Master agreements are typically used to facilitate the netting of cash flows associated with a single counterparty and may include collateral requirements. Collateral requirements in the form of cash, letters of credit, surety bonds and parental/affiliate guarantees may be obtained as security from counterparties in order to mitigate credit risk. Some master agreements include margining, which requires a counterparty to post cash or letters of credit in the event exposure exceeds the established threshold. The threshold represents an unsecured credit limit which may be supported by a parental/affiliate guaranty, as determined in accordance with AEP's credit policy. In addition, master agreements allow for termination and liquidation of all positions in the event of a default including failure or inability to post collateral when required.

Collateral Triggering Events

Credit Downgrade Triggers

A limited number of derivative contracts include collateral triggering events, which include a requirement to maintain certain credit ratings. On an ongoing basis, AEP's risk management organization assesses the appropriateness of these collateral triggering events in contracts. KPCo has not experienced a downgrade below a specified credit rating threshold that would require the posting of additional collateral. As of September 30, 2021 and December 31, 2020, KPCo did not have derivative contracts with collateral triggering events in a net liability position.

Cross-Default Triggers

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

	September 30, 2021	**December 31, 2020**
	(in thousands)	
Liabilities for Contracts with Cross-Default Provisions Prior to Contractual Netting Arrangements	$ 181	$ 154
Additional Settlement Liability if Cross-Default Provision is Triggered	8	16

8. FAIR VALUE MEASUREMENTS

Fair Value Hierarchy and Valuation Techniques

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

For commercial activities, exchange-traded derivatives, namely futures contracts, are generally fair valued based on unadjusted quoted prices in active markets and are classified as Level 1. Level 2 inputs primarily consist of OTC broker quotes in moderately active or less active markets, as well as exchange-traded derivatives where there is insufficient market liquidity to warrant inclusion in Level 1. Management verifies price curves using these broker quotes and classifies these fair values within Level 2 when substantially all of the fair value can be corroborated. Management typically obtains multiple broker quotes, which are nonbinding in nature but are based on recent trades in the marketplace. When multiple broker quotes are obtained, the quoted bid and ask prices are averaged. In certain circumstances, a broker quote may be discarded if it is a clear outlier. Management uses a historical correlation analysis between the broker quoted location and the illiquid locations. If the points are highly correlated, these locations are included within Level 2 as well. Certain OTC and bilaterally executed derivative instruments are executed in less active markets with a lower availability of pricing information. Illiquid transactions, complex structured transactions, FTRs and counterparty credit risk may require nonmarket-based inputs. Some of these inputs may be internally developed or extrapolated and utilized to estimate fair value. When such inputs have a significant impact on the measurement of fair value, the instrument is categorized as Level 3. The main driver of contracts being classified as Level 3 is the inability to substantiate energy price curves in the market. A portion of the Level 3 instruments have been economically hedged which limits potential earnings volatility.

Fair Value Measurements of Long-term Debt

The fair values of Long-term Debt are based on quoted market prices, without credit enhancements, for the same or similar issues and the current interest rates offered for instruments with similar maturities classified as Level 2 measurement inputs. These instruments are not marked-to-market. The estimates presented are not necessarily indicative of the amounts that could be realized in a current market exchange.

The book values and fair values of KPCo's Long-term Debt are summarized in the following table:

	September 30, 2021		December 31, 2020	
	Book Value	Fair Value	Book Value	Fair Value
	(in thousands)			
Long-term Debt	$ 1,102,989	$ 1,236,313	$ 992,650	$ 1,166,298

Fair Value Measurements of Financial Assets and Liabilities

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

Assets and Liabilities Measured at Fair Value on a Recurring Basis
September 30, 2021

	Level 1	Level 2	Level 3	Other	Total
			(in thousands)		
Assets:					
Risk Management Assets					
Risk Management Commodity Contracts (a) (b)	$ —	$ 9,304	$ 5,999	$ (9,545)	$ 5,758
Liabilities:					
Risk Management Liabilities					
Risk Management Commodity Contracts (a) (b)	$ —	$ 12,352	$ 447	$ (12,531)	$ 268

December 31, 2020

	Level 1	Level 2	Level 3	Other	Total
			(in thousands)		
Assets:					
Risk Management Assets					
Risk Management Commodity Contracts (a) (b)	$ —	$ 3,669	$ 3,204	$ (3,698)	$ 3,175
Liabilities:					
Risk Management Liabilities					
Risk Management Commodity Contracts (a) (b)	$ —	$ 3,655	$ 179	$ (3,602)	$ 232

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

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

Three Months Ended September 30, 2021	Net Risk Management Assets (Liabilities) (in thousands)
Balance as of June 30, 2021	$ 6,355
Realized Gain (Loss) Included in Net Income (or Changes in Net Assets) (a) (b)	2,598
Settlements	(4,310)
Transfers out of Level 3 (c)	13
Changes in Fair Value Allocated to Regulated Jurisdictions (d)	896
Balance as of September 30, 2021	$ 5,552

Three Months Ended September 30, 2020	Net Risk Management Assets (Liabilities) (in thousands)
Balance as of June 30, 2020	$ 6,301
Realized Gain (Loss) Included in Net Income (or Changes in Net Assets) (a) (b)	3,151
Settlements	(4,633)
Changes in Fair Value Allocated to Regulated Jurisdictions (d)	125
Balance as of September 30, 2020	$ 4,944

Nine Months Ended September 30, 2021	Net Risk Management Assets (Liabilities) (in thousands)
Balance as of December 31, 2020	$ 3,025
Realized Gain (Loss) Included in Net Income (or Changes in Net Assets) (a) (b)	1,981
Settlements	(5,039)
Transfers out of Level 3 (c)	8
Changes in Fair Value Allocated to Regulated Jurisdictions (d)	5,577
Balance as of September 30, 2021	$ 5,552

Nine Months Ended September 30, 2020	Net Risk Management Assets (Liabilities) (in thousands)
Balance as of December 31, 2019	$ 5,702
Realized Gain (Loss) Included in Net Income (or Changes in Net Assets) (a) (b)	4,073
Settlements	(9,856)
Transfers out of Level 3 (c)	130
Changes in Fair Value Allocated to Regulated Jurisdictions (d)	4,895
Balance as of September 30, 2020	$ 4,944

(a) Included in revenues on KPCo’s statements of income.
(b) Represents the change in fair value between the beginning of the reporting period and the settlement of the risk management commodity contract.
(c) Transfers are recognized based on their value at the beginning of the reporting period that the transfer occurred.
(d) Relates to the net gains (losses) of those contracts that are not reflected on KPCo’s statements of income. These net gains (losses) are recorded as regulatory assets/liabilities or accounts payable.

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

Significant Unobservable Inputs
September 30, 2021

	Fair Value		Valuation	Significant Unobservable	Input/Range		
	Assets	Liabilities	Technique	Input (a)	Low	High	Weighted Average (b)
	(in thousands)						
Energy Contracts	$ 44	$ 210	Discounted Cash Flow	Forward Market Price	$ 26.70	$ 87.14	$ 53.61
FTRs	5,955	237	Discounted Cash Flow	Forward Market Price	0.17	7.68	1.05
Total	$ 5,999	$ 447					

December 31, 2020

	Fair Value		Valuation	Significant Unobservable	Input/Range		
	Assets	Liabilities	Technique	Input (a)	Low	High	Weighted Average (b)
	(in thousands)						
Energy Contracts	$ 190	$ 121	Discounted Cash Flow	Forward Market Price	$ 10.84	$ 41.09	$ 25.08
FTRs	3,014	58	Discounted Cash Flow	Forward Market Price	0.17	4.18	1.03
Total	$ 3,204	$ 179					

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

The following table provides the measurement uncertainty of fair value measurements to increases (decreases) in significant unobservable inputs related to Energy Contracts and FTRs as of September 30, 2021 and December 31, 2020:

Uncertainty of Fair Value Measurements

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

9. INCOME TAXES

Effective Tax Rates (ETR)

KPCo's interim ETR reflects the estimated annual ETR for 2021 and 2020, adjusted for tax expense associated with certain discrete items.

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

The ETR for KPCo is included in the following table:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2020	2021	2020
U.S. Federal Statutory Rate	21.0 %	21.0 %	21.0 %	21.0 %
Increase (decrease) due to:				
State Income Tax, net of Federal Benefit	(34.6)%	(5.0)%	(17.7)%	(5.0)%
Tax Reform Excess ADIT Reversal	(98.5)%	(30.2)%	(117.9)%	(30.2)%
Flow Through	(2.0)%	0.3 %	(1.9)%	0.3 %
AFUDC Equity	(0.7)%	(2.0)%	(1.1)%	(2.0)%
Discrete Tax Adjustments	— %	(7.1)%	— %	(4.4)%
Other	0.4 %	0.1 %	— %	— %
Effective Income Tax Rate	(114.4)%	(22.9)%	(117.6)%	(20.3)%

Federal and State Income Tax Audit Status

The statute of limitations for the IRS to examine KPCo and other AEP subsidiaries originally filed federal return has expired for tax years 2016 and earlier. In the third quarter of 2019, KPCo and other AEP subsidiaries elected to amend the 2014 through 2017 federal returns. In the first quarter of 2020, the IRS notified AEP that it was beginning an examination of these amended returns, including the net operating loss carryback to 2015 that originated in the 2017 return. As of September 30, 2021, the IRS has not challenged any items on these returns and the IRS is limited in their proposed adjustments to the amount AEP claimed on the amended returns. AEP has agreed to extend the statute of limitations on the 2017 tax return to December 31, 2022 to allow time for the audit to be completed and the Congressional Joint Committee on Taxation to approve the associated refund claim.

10. FINANCING ACTIVITIES

Long-term Debt

Long-term debt issued during the first nine months of 2021 is shown in the following table:

Type of Issuance	Principal Amount (a)	Interest Rate	Due Date
	(in thousands)	(%)	
Other Long-term Debt	$ 150,000	Variable	2023

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

Long-term debt retired during the first nine months of 2021 is shown in the following table:

Type of Retirement	Principal Amount	Interest Rate	Due Date
	(in thousands)	(%)	
Senior Unsecured Notes	$ 40,000	7.25	2021

Dividend Restrictions

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

All of the dividends declared by KPCo are subject to a Federal Power Act restriction that prohibits the payment of dividends out of capital accounts without regulatory approval; payment of dividends is allowed out of retained earnings only.

KPCo has credit agreements that contain a covenant that limit its debt to capitalization ratio to 67.5%. As of September 30, 2021, KPCo did not exceed its debt to capitalization limit. The method for calculating outstanding debt and capitalization is contractually-defined in the credit agreements.

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

Corporate Borrowing Program – AEP System

The AEP System uses a corporate borrowing program to meet the short-term borrowing needs of AEP's subsidiaries. The corporate borrowing program includes a Utility Money Pool, which funds AEP's utility subsidiaries. The AEP System Utility Money Pool operates in accordance with the terms and conditions of its agreement filed with the FERC. The amounts of outstanding borrowings from the Utility Money Pool as of September 30, 2021 and December 31, 2020 are included in Advances from Affiliates on KPCo's balance sheets. KPCo's Utility Money Pool activity and corresponding authorized borrowing limit for the nine months ended September 30, 2021 are described in the following table:

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	Borrowings from the Utility Money Pool as of September 30, 2021	Authorized Short-Term Borrowing Limit
		(in thousands)			
$ 121,608	$ 43,730	$ 53,609	$ 22,427	$ 13,811	$ 180,000

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

Nine Months Ended September 30,	Maximum Interest Rate for Funds Borrowed from the Utility Money Pool	Minimum Interest Rate for Funds Borrowed from the Utility Money Pool	Maximum Interest Rate for Funds Loaned to the Utility Money Pool	Minimum Interest Rate for Funds Loaned to the Utility Money Pool	Average Interest Rate for Funds Borrowed from the Utility Money Pool	Average Interest Rate for Funds Loaned to the Utility Money Pool
2021	0.40 %	0.02 %	0.34 %	0.03 %	0.32 %	0.33 %
2020	2.70 %	0.33 %	2.08 %	1.80 %	1.49 %	1.81 %

Securitized Accounts Receivables – AEP Credit

Under an affiliated receivables sales arrangement, KPCo sells, without recourse, certain of its customer accounts receivable and accrued unbilled revenue balances to AEP Credit. KPCo is charged a fee for each sale that is based on AEP Credit's financing costs, administrative costs and uncollectible accounts experience from previous purchases of KPCo's customer accounts receivable. No allowance for uncollectible accounts is recognized within KPCo's financial statements for customer accounts receivable sold to AEP Credit, and any bad debt stemming from these receivables would be recognized by AEP Credit. The costs of customer accounts receivable sold are reported in Other Operation expense on KPCo's statements of income. KPCo manages and services its accounts receivable sold.

AEP Credit's receivables securitization agreement provides a commitment of $750 million from bank conduits to purchase receivables and was amended in September 2021 to include a $125 million and a $625 million facility, which expire in September 2023 and 2024, respectively. As of September 30, 2021, KPCo was in compliance with all requirements under the agreement.

KPCo's amounts of accounts receivable and accrued unbilled revenues sold under the sale of receivables agreement were $43.6 million and $54.8 million as of September 30, 2021 and December 31, 2020, respectively.

The fees paid by KPCo to AEP Credit for customer accounts receivable sold for the three months ended September 30, 2021 and 2020 were $1.2 million and $2.4 million, respectively, and for the nine months ended September 30, 2021 and 2020 were $868 thousand and $4.4 million, respectively. In 2020, an increase in allowance for doubtful accounts was recognized in response to the anticipated impact of COVID-19 on the collectability of accounts receivable, which caused an increase in fees paid by KPCo. In 2021, due to higher than expected collections of accounts receivables, allowance for doubtful accounts was adjusted resulting in the issuance of credits to offset the higher fees previously paid and to lower subsequent fees paid.

KPCo's proceeds on the sale of receivables to AEP Credit for the three months ended September 30, 2021 and 2020 were $150.9 million and $123.4 million, respectively, and for the nine months ended September 30, 2021 and 2020 were $443.4 million and $375.9 million, respectively.

11. PROPERTY, PLANT AND EQUIPMENT

Asset Retirement Obligations (ARO)

KPCo 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 aggregate carrying amounts of ARO for KPCo:

ARO as of December 31, 2020	Accretion Expense	Liabilities Incurred	Liabilities Settled	Revisions in Cash Flow Estimates	ARO as of September 30, 2021
		(in thousands)			
$ 24,565	$ 757	$ —	$ (621)	$ (3,812)	$ 20,889

12. REVENUE FROM CONTRACTS WITH CUSTOMERS

Disaggregated Revenues from Contracts with Customers

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

	Three Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
	(in thousands)			
Retail Revenues:				
Residential Revenues	$ 71,581	$ 59,767	$ 209,907	$ 174,709
Commercial Revenues	40,806	35,920	117,032	102,310
Industrial Revenues	34,614	28,167	102,222	90,161
Other Retail Revenues	486	450	1,485	1,407
Total Retail Revenues	147,487	124,304	430,646	368,587
Wholesale Revenues:				
Generation Revenues (a)	11,007	4,837	25,630	11,131
Transmission Revenues (b)	5,602	5,792	16,522	17,225
Total Wholesale Revenues	16,609	10,629	42,152	28,356
Other Revenues from Contracts with Customers (a)	2,167	2,495	6,416	10,504
Total Revenues from Contracts with Customers	166,263	137,428	479,214	407,447
Other Revenues:				
Alternative Revenues	(220)	124	(1,494)	514
Total Other Revenues	(220)	124	(1,494)	514
Total Revenues	$ 166,043	$ 137,552	$ 477,720	$ 407,961

(a) Amounts include affiliated and nonaffiliated revenues.
(b) Amounts include affiliated and nonaffiliated revenues. The affiliated revenues were $2.2 million and $2.7 million for the three months ended September 30, 2021 and 2020, respectively, and $6.7 million and $8 million for the nine months ended September 30, 2021 and 2020, respectively.

Fixed Performance Obligations

The following table represents KPCo's remaining fixed performance obligations satisfied over time as of September 30, 2021. Fixed performance obligations primarily include wholesale transmission services, electricity sales for fixed amounts of energy and stand ready services into PJM's Reliability Pricing Model market. The amounts shown in the table below include affiliated and nonaffiliated revenues.

2021	2022-2023	2024-2025	After 2025	Total
		(in thousands)		
$ 6,846	$ 5,149	$ 2,870	$ 1,435	$ 16,300

Contract Assets and Liabilities

Contract assets are recognized when KPCo has a right to consideration that is conditional upon the occurrence of an event other than the passage of time, such as future performance under a contract. KPCo did not have material contract assets as of September 30, 2021 and December 31, 2020.

When KPCo receives consideration, or such consideration is unconditionally due from a customer prior to transferring goods or services to the customer under the terms of a sales contract, they recognize a contract liability on the balance sheet in the amount of that consideration. Revenue for such consideration is subsequently recognized in the period or periods in which the remaining performance obligations in the contract are satisfied. KPCo's contract liabilities typically arise from advanced payments of services provided primarily with respect to joint use agreements for utility poles. KPCo did not have material contract liabilities as of September 30, 2021 and December 31, 2020.

Accounts Receivable from Contracts with Customers

Accounts receivable from contracts with customers are presented on KPCo's balance sheets within the Accounts Receivable - Customers line item. KPCo's balances for receivables from contracts that are not recognized in accordance with the accounting guidance for "Revenue from Contracts with Customers" included in Accounts Receivable - Customers were not material as of September 30, 2021 and December 31, 2020. See "Securitized Accounts Receivable - AEP Credit" section of Note 10 for additional information related to AEP Credit's securitized accounts receivable.

The amount of affiliated accounts receivable from contracts with customers included in Accounts Receivable - Affiliated Companies on KPCo's balance sheets were $7.2 million and $8.3 million, respectively, as of September 30, 2021 and December 31, 2020.

13. SUBSEQUENT EVENTS

Disposition of KPCo and KTCo

In October 2021, AEP entered into a Stock Purchase Agreement to sell KPCo and AEP Kentucky Transco to Liberty Utilities Co., a subsidiary of Algonquin Power & Utilities Corp. (Liberty), for approximately a $2.85 billion enterprise value. The sale is subject to regulatory approvals from the FERC, the KPSC, clearance under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, and clearance from the Committee on Foreign Investment in the United States.

KPCo currently operates and owns a 50% interest in the 1,560 MW coal-fired Mitchell Power Plant (Mitchell Plant) with the remaining 50% owned by WPCo. The Stock Purchase Agreement is further contingent upon approval by the KPSC and the WVPSC of a new proposed Mitchell Plant Operating Agreement and Mitchell Plant Ownership Agreement between KPCo and WPCo pursuant to which WPCo will replace KPCo as the operator of the Mitchell Plant and KPCo employees at the Mitchell Plant will become employees of WPCo at closing of the transaction. Under the proposed Ownership Agreement, WPCo is obligated to purchase KPCo's 50% interest in the Mitchell Plant on December 31, 2028 unless KPCo and WPCo have agreed to retire the Mitchell Plant earlier or, absent such agreement, if WPCo elects prior to December 31, 2027 to retire the Mitchell Plant on December 31, 2028. The Ownership Agreement provides that the purchase price for KPCo's 50% ownership interest in the Mitchell Plant will be determined through the mutual agreement of WPCo and KPCo (subject to approval from the KPSC and WVPSC) or through a fair market valuation determination conducted by independent appraisals if KPCo and WPCo are unable to reach agreement as to the purchase price.

The sale is expected to close in the second quarter of 2022 with Liberty acquiring the assets and assuming the liabilities of KPCo and AEP Kentucky Transco, excluding pension and other post-retirement benefit plan assets and liabilities. AEP expects to provide customary transition services to Liberty for a period of time after closing of the transaction.