

## **TRANSMISSION AND DISTRIBUTION UTILITIES**

### **GENERAL**

This segment consists of the transmission and distribution of electricity for sale to retail and wholesale customers through assets owned and operated by AEP Texas and OPCo. OPCo is engaged in the transmission and distribution of electric power to approximately 1,494,000 retail customers in Ohio. OPCo purchases energy and capacity at auction to serve generation service customers who have not switched to a competitive generation supplier. AEP Texas is engaged in the transmission and distribution of electric power to approximately 1,049,000 retail customers through REPs in west, central and southern Texas.

AEP's transmission and distribution utility subsidiaries own and operate transmission and distribution lines and other facilities to deliver electric power. See Item 2 - Properties, for more information regarding the transmission and distribution lines. Transmission and distribution services are sold to retail customers of AEP's transmission and distribution utility subsidiaries in their service territories. These sales are made at rates approved by the PUCT for AEP Texas and by the PUCO and the FERC for OPCo. The FERC regulates and approves the rates for wholesale transmission transactions. As discussed below, some transmission services also are separately sold to nonaffiliated companies.

AEP's transmission and distribution utility subsidiaries hold franchises or other rights to provide electric service in various municipalities and regions in their service areas. In some cases, these franchises provide the utility with the exclusive right to provide electric service. These franchises have varying provisions and expiration dates. In general, the operating companies consider their franchises to be adequate for the conduct of their business.

The use and the recovery of costs associated with the transmission assets of the AEP transmission and distribution utility subsidiaries are subject to the rules, protocols and agreements in place with PJM and ERCOT, and as approved by the FERC. In addition to providing transmission services in connection with power sales in their service areas, AEP's transmission and distribution utility subsidiaries also provide transmission services for nonaffiliated companies through RTOs.

#### ***Transmission Agreement***

OPCo owns and operates transmission facilities that are used to provide transmission service under the PJM OATT; OPCo is a party to the TA with other utility subsidiary affiliates. The TA defines how the parties to the agreement share the revenues associated with their transmission facilities and the costs of transmission service provided by PJM. The TA has been approved by the FERC.

#### ***Regional Transmission Organizations***

OPCo is a member of PJM, a FERC-approved RTO. RTOs operate, plan and control utility transmission assets to provide open access to such assets in a way that prevents discrimination between participants owning transmission assets and those that do not. AEP Texas is a member of ERCOT.

### **REGULATION**

OPCo provides distribution and transmission services to retail customers within its service territory at cost-based rates approved by the PUCO or by the FERC. AEP Texas provides transmission and distribution service on a cost-of-service basis at rates approved by the PUCT and wholesale transmission service under tariffs approved by the FERC consistent with PUCT rules. Transmission and distribution rates are established on a cost-of-service basis, which is designed to allow a utility an opportunity to recover its cost of providing service and to earn a reasonable return on its investment used in providing that service. The cost of service generally reflects operating expenses, including operation and maintenance expense, depreciation expense and taxes. Utility commissions periodically adjust rates pursuant to a review of: (a) a utility's adjusted revenues and expenses during a defined test period and (b) such utility's level of investment.