PENNSYLVANIA ELECTRIC COMPANY AND SUBSIDIARY

AUDITED CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018

GLOSSARY OF TERMS

The following abbreviations and acronyms may be used in these financial statements to identify Pennsylvania Electric Company and its current and former subsidiaries and affiliated companies:

ATSI	American Transmission Systems, Incorporated, formerly a direct subsidiary of FE that became a subsidiary of FET in April 2012, which owns and operates transmission facilities
CEI	The Cleveland Electric Illuminating Company, an Ohio electric utility operating affiliated company
FE	FirstEnergy Corp., a public utility holding company
FES	FirstEnergy Solutions Corp., together with its consolidated subsidiaries, which provides energy-related products and services. On March 31, 2018, FES filed voluntary petitions under Chapter 11 of the United States Bankruptcy Code with the Bankruptcy Court. FES was deconsolidated from FirstEnergy's consolidated financial statements as of March 31, 2018.
FESC	FirstEnergy Service Company, which provides legal, financial and other corporate support services
FET	FirstEnergy Transmission, LLC, formerly known as Allegheny Energy Transmission, LLC, which is the parent of ATSI, MAIT and TrAIL and has a joint venture in PATH
FirstEnergy	FirstEnergy Corp., together with its consolidated subsidiaries
GPU	GPU, Inc., former parent of JCP&L, ME and PN, that merged with FE on November 7, 2001
JCP&L	Jersey Central Power & Light Company, a New Jersey electric utility operating affiliated company
MAIT	Mid-Atlantic Interstate Transmission, LLC, a subsidiary of FET, which owns and operates transmission facilities
ME	Metropolitan Edison Company, a Pennsylvania electric utility operating affiliated company
MP	Monongahela Power Company, a West Virginia electric utility operating affiliated company
OE	Ohio Edison Company, an Ohio electric utility operating affiliated company
PATH	Potomac-Appalachian Transmission Highline, LLC, a joint venture between FE and a subsidiary of AEP
PE	The Potomac Edison Company, a Maryland electric utility operating affiliated company
Penn	Pennsylvania Power Company, a Pennsylvania electric utility operating subsidiary of OE
Pennsylvania Companies	ME, PN, Penn and WP
PN	Pennsylvania Electric Company, a Pennsylvania electric utility operating company
TE	The Toledo Edison Company, an Ohio electric utility operating affiliated company
TrAIL	Trans-Allegheny Interstate Line Company, a subsidiary of FET, which owns and operates transmission facilities
Utilities	OE, CEI, TE, Penn, JCP&L, ME, PN, MP, PE and WP
WP	West Penn Power Company, a Pennsylvania electric utility operating affiliated company

The following abbreviations and acronyms may be used to identify frequently used terms in these financial statements:

ADIT	Accumulated Deferred Income Taxes
AEP	American Electric Power Company, Inc.
AFS	Available-for-sale
AFUDC	Allowance for Funds Used During Construction
ALJ	Administrative Law Judge
ANI	American Nuclear Insurers
AOCI	Accumulated Other Comprehensive Income
ARO	Asset Retirement Obligation
ASU	Accounting Standards Update
DSIC	Distribution System Improvement Charge
DSP	Default Service Plan
EDC	Electric Distribution Company
EE&C	Energy Efficiency and Conservation
EGS	Electric Generation Supplier
ERO	Electric Reliability Organization

GLOSSARY OF TERMS, *Continued*

FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
FPA	Federal Power Act
GAAP	Accounting Principles Generally Accepted in the United States of America
ICE	IntercontinentalExchange, Inc.
IRS	Internal Revenue Service
kV	Kilovolt
LTIIP	Long-Term Infrastructure Improvement Plans
MLP	Master Limited Partnership
MWH	Megawatt-hour
NDT	Nuclear Decommissioning Trust
NEIL	Nuclear Electric Insurance Limited
NERC	North American Electric Reliability Corporation
NOL	Net Operating Loss
NRC	Nuclear Regulatory Commission
NUG	Non-Utility Generation
NYPSC	New York State Public Service Commission
OPEB	Other Post-Employment Benefits
PJM	PJM Interconnection, L.L.C.
PJM Region	The aggregate of the zones within PJM
PJM Tariff	PJM Open Access Transmission Tariff
POLR	Provider of Last Resort
POR	Purchase of Receivables
PPUC	Pennsylvania Public Utility Commission
PURPA	Public Utility Regulatory Policies Act of 1978
RFC	Reliability*First* Corporation
RFP	Request for Proposal
ROE	Return on Equity
SREC	Solar Renewable Energy Credit
Tax Act	Tax Cuts and Jobs Act adopted December 22, 2017
TMI-2	Three Mile Island Unit 2
VIE	Variable Interest Entity

Report of Independent Auditors

To Management and the Board of Directors
Of Pennsylvania Electric Company

We have audited the accompanying consolidated financial statements of Pennsylvania Electric Company and its subsidiary (the "Company"), which comprise the consolidated balance sheets as of December 31, 2019 and 2018, and the related consolidated statements of income and comprehensive income, of common stockholder's equity, and of cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Pennsylvania Electric Company and its subsidiary as of December 31, 2019 and 2018, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

/s/ PricewaterhouseCoopers LLP
Cleveland, Ohio
March 4, 2020

PENNSYLVANIA ELECTRIC COMPANY AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(In millions)	For the Years Ended December 31, 2019	2018
REVENUES:		
Electric sales	$ 832	$ 866
Gross receipts tax collections	49	49
Total revenues	881	915
OPERATING EXPENSES:		
Purchased power from affiliates	14	30
Purchased power from non-affiliates	290	290
Other operating expenses	203	209
Provision for depreciation	94	87
Deferral of regulatory liabilities, net	3	18
General taxes	57	58
Total operating expenses	661	692
OPERATING INCOME	220	223
OTHER INCOME (EXPENSE):		
Miscellaneous income, net	18	20
Equity earnings from MAIT	36	31
Pension and OPEB mark-to-market adjustment	(41)	(3)
Interest expense	(61)	(60)
Capitalized financing costs	3	1
Total other expense	(45)	(11)
INCOME BEFORE INCOME TAXES	175	212
INCOME TAXES	27	40
NET INCOME	$ 148	$ 172
STATEMENTS OF COMPREHENSIVE INCOME		
NET INCOME	$ 148	$ 172
OTHER COMPREHENSIVE LOSS:		
Pension and OPEB prior service costs	(2)	(4)
Other comprehensive loss	(2)	(4)
Income tax benefits on other comprehensive loss	(1)	(3)
Other comprehensive loss, net of tax	(1)	(1)
COMPREHENSIVE INCOME	$ 147	$ 171

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

PENNSYLVANIA ELECTRIC COMPANY AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

(In millions, except share amounts)	December 31, 2019	December 31, 2018
ASSETS		
CURRENT ASSETS:		
Receivables-		
Customers, net of allowance for uncollectible accounts of $7 in 2019 and 2018	$ 137	$ 143
Affiliated companies	21	14
Other	11	25
Notes receivable from affiliated companies	85	—
Prepaid taxes and other	12	12
	266	194
UTILITY PLANT:		
In service	3,227	3,098
Less — Accumulated provision for depreciation	1,075	1,028
	2,152	2,070
Construction work in progress	78	68
	2,230	2,138
OTHER PROPERTY AND INVESTMENTS:		
Nuclear plant decommissioning trusts (Note 13)	—	191
Investment in affiliate	450	451
Other	1	2
Investments - held for sale (Note 13)	215	—
	666	644
DEFERRED CHARGES AND OTHER ASSETS:		
Goodwill	637	637
Other	28	8
	665	645
	$ 3,827	$ 3,621
LIABILITIES AND CAPITALIZATION		
CURRENT LIABILITIES:		
Currently payable long-term debt	$ 253	$ 128
Short-term borrowings - affiliated companies	—	50
Accounts payable-		
Affiliated companies	3	7
Other	50	50
Accrued taxes	10	12
Accrued interest	13	14
Customer deposits	25	24
Other	21	21
	375	306
CAPITALIZATION:		
Common stockholder's equity-		
Common stock, $20 par value, authorized 5,400,000 shares - 4,427,577 shares outstanding	89	89
Other paid-in capital	1,049	1,046
Accumulated other comprehensive income	4	5
Retained earnings	176	173
Total common stockholder's equity	1,318	1,313
Long-term debt and other long-term obligations	1,047	1,003
	2,365	2,316
NONCURRENT LIABILITIES:		
Accumulated deferred income taxes	301	277
Retirement benefits	165	147
Regulatory liabilities	225	192
Asset retirement obligations (Note 13)	4	167
Power purchase contract liability	16	44
Other	204	172
Noncurrent liabilities - held for sale (Note 13)	172	—
	1,087	999
COMMITMENTS AND CONTINGENCIES (NOTE 13)		
	$ 3,827	$ 3,621

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

PENNSYLVANIA ELECTRIC COMPANY AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMMON STOCKHOLDER'S EQUITY

(In millions, except share amounts)	Common Stock: Number of Shares	Common Stock: Carrying Value	Other Paid-In Capital	AOCI	Retained Earnings	Total Stockholder's Equity
Balance, January 1, 2018	4,427,577	$ 89	$ 1,043	$ 6	$ 82	$ 1,220
Net income					172	172
Other comprehensive loss, net of tax				(1)		(1)
Consolidated tax benefit allocation			1			1
Stock-based compensation			2			2
Impact of adopting ASU 2018-02 (1)					(1)	(1)
Cash dividends declared on common stock					(80)	(80)
Balance, December 31, 2018	4,427,577	$ 89	$ 1,046	$ 5	$ 173	$ 1,313
Net income					148	148
Other comprehensive loss, net of tax				(1)		(1)
Consolidated tax benefit allocation			1			1
Stock-based compensation			2			2
Cash dividends declared on common stock					(145)	(145)
Balance, December 31, 2019	4,427,577	$ 89	$ 1,049	$ 4	$ 176	$ 1,318

(1) PN early adopted ASU 2018-02, "Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income" during the first quarter of 2018. Upon adoption, PN recorded a cumulative effect adjustment for stranded tax effects, such as pension and OPEB prior service costs to retained earnings.

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

PENNSYLVANIA ELECTRIC COMPANY AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)	For the Years Ended December 31, 2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 148	$ 172
Adjustments to reconcile net income to net cash from operating activities-		
Depreciation and amortization	97	111
Deferred income taxes and investment tax credits, net	7	26
Pension trust contributions	(1)	(65)
Retirement benefits, net of payments	(12)	(18)
Pension and OPEB mark-to-market adjustment	41	3
Undistributed earnings from subsidiary company	2	(2)
Change in current assets and liabilities-		
Receivables	14	2
Accounts payable	(4)	(2)
Accrued taxes	(2)	(5)
Accrued interest	(1)	—
Customer deposits	1	3
Other current liabilities	(3)	2
Other	2	23
Net cash provided from operating activities	289	250
CASH FLOWS FROM FINANCING ACTIVITIES:		
New financing-		
Long-term debt	300	—
Short-term borrowings - affiliated companies, net	—	27
Redemptions and repayments-		
Long-term debt	(125)	—
Short-term borrowings - affiliated companies, net	(50)	—
Common stock dividend payments	(145)	(80)
Debt issuance costs	(3)	—
Other	(4)	(4)
Net cash used for financing activities	(27)	(57)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Property additions	(157)	(172)
Loans to affiliated companies, net	(85)	—
Sales of investment securities held in trusts	366	154
Purchases of investment securities held in trusts	(373)	(161)
Asset removal costs	(13)	(14)
Net cash used for investing activities	(262)	(193)
Net change in cash, cash equivalents, and restricted cash	—	—
Cash, cash equivalents, and restricted cash at beginning of period	—	—
Cash, cash equivalents, and restricted cash at end of period	$ —	$ —
SUPPLEMENTAL CASH FLOW INFORMATION:		
Cash paid during the year-		
Interest (net of amounts capitalized)	$ 60	$ 59
Income taxes, net of refunds	$ 30	$ —

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

PENNSYLVANIA ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND BASIS OF PRESENTATION

Unless otherwise indicated, defined terms and abbreviations used herein have the meanings set forth in the accompanying Glossary of Terms.

PN, together with its consolidated subsidiary is a wholly owned subsidiary of FE and is incorporated in Pennsylvania. PN operates an electric distribution system in Pennsylvania and New York. PN is subject to regulation by the PPUC, NYPSC and FERC. Additionally, as discussed in "Investment in Unconsolidated Affiliate" below, PN transferred its transmission assets to MAIT on January 31, 2017.

PN follows GAAP and complies with the regulations, orders, policies and practices prescribed by FERC, PPUC and the NYPSC. The preparation of financial statements in conformity with GAAP requires management to make periodic estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities. Actual results could differ from these estimates. The reported results of operations are not necessarily indicative of results of operations for any future period. PN has evaluated events and transactions for potential recognition or disclosure through March 4, 2020, the date the financial statements were issued.

CUSTOMER RECEIVABLES

PN's principal business is providing electric service to customers in Pennsylvania. PN's retail customers are metered on a cycle basis. Electric revenues are recorded based on energy delivered through the end of the calendar month. An estimate of unbilled revenues is calculated to recognize electric service provided from the last meter reading through the end of the month. This estimate includes many factors, among which are historical customer usage, load profiles, estimated weather impacts, customer shopping activity and prices in effect for each class of customer. In each accounting period, PN accrues the estimated unbilled amount as revenue and reverses the related prior period estimate.

Receivables from customers include retail electric sales and distribution deliveries to residential, commercial and industrial customers. The allowance for uncollectible customer receivables is based on historical loss information comprised of a rolling 36-month average net write-off percentage of revenues. Billed and unbilled customer receivables were $81 million and $56 million, respectively, as of December 31, 2019 and $89 million and $54 million, respectively, as of December 31, 2018. There was no material concentration of receivables as of December 31, 2019 and 2018, with respect to any particular segment of PN's customers.

ACCOUNTING FOR THE EFFECTS OF REGULATION

Regulatory assets represent incurred costs that have been deferred because of their probable future recovery from customers through regulated rates. Regulatory liabilities represent amounts that are expected to be credited to customers through future regulated rates or amounts collected from customers for costs not yet incurred. PN nets its regulatory assets and liabilities based on federal and state jurisdictions. PN considers the entire regulatory asset balance as the unit of account for the purposes of balance sheet classification rather than the next years recovery and as such net regulatory assets and liabilities are presented in the non-current section on the PN Balance Sheets.

Management assesses the probability of recovery of regulatory assets at each balance sheet date and whenever new events occur. Similarly, Management records regulatory liabilities when a determination is made that a refund is probable or when ordered by a commission. Factors that may affect probability include changes in the regulatory environment, issuance of a regulatory commission order or passage of new legislation. If recovery of a regulatory asset is no longer probable, that regulatory asset is written off as a charge against earnings. Management applies judgment in evaluating the evidence available to assess the probability of recovery of regulatory assets from customers, including, but not limited to evaluating evidence related to precedent for similar items at the Company and information on comparable companies within similar jurisdictions, as well as assessing progress of communications between the Company and regulators.

The following table provides information about the composition of net regulatory assets and liabilities as of December 31, 2019 and December 31, 2018, and the changes during the year ended December 31, 2019:

Net Regulatory Assets (Liabilities) by Source	December 31, 2019	December 31, 2018	Change
		(In millions)	
Regulatory transition costs	$ (16)	$ (13)	$ (3)
Customer payables for future income taxes	(176)	(189)	13
Nuclear decommissioning and spent fuel disposal costs	(47)	(32)	(15)
Asset removal costs	(2)	(4)	2
Deferred transmission costs	(21)	(30)	9
Deferred generation costs	(9)	(14)	5
Deferred distribution costs	6	19	(13)
Contract valuations	16	44	(28)
Storm-related costs	25	22	3
Other	(1)	5	(6)
Net Regulatory Liabilities included on the Consolidated Balance Sheets	$ (225)	$ (192)	$ (33)

The following is a description of the regulatory assets and liabilities described above:

Regulatory transition costs - Primarily relates to above market NUG costs.

Customer payables for future income taxes - Reflects amounts to be recovered or refunded through future rates to pay income taxes that become payable when rate revenue is provided to recover items such as AFUDC-equity and depreciation of property, plant and equipment for which deferred income taxes were not recognized for ratemaking purposes, including amounts attributable to tax rate changes such as the Tax Act. These amounts are being amortized over the period in which the related deferred tax asset reverse, which is generally over the expected life of the underlying asset. See Note 5, "Taxes" for further discussion on the Tax Act.

Nuclear decommissioning and spent fuel disposal costs - Reflects a regulatory liability representing amounts collected from customers and placed in external trusts including income, losses and changes in fair value thereon (as well as accretion of the related ARO) for the future decommissioning of TMI-2.

Asset removal costs - Primarily represents the recovery of asset removal costs incurred that are amortized on a five year average.

Deferred transmission costs - Primarily relates to the recovery of non-market based costs or fees imposed on or charged to PN by various regulatory bodies including FERC, the state of Pennsylvania and regional transmission organizations. These costs can include PJM charges and credits for service including, but not limited to, procuring transmission services and transmission enhancement.

Deferred generation costs - Relates to the costs to provide energy and capacity services to customers who take default services including non market based transmission and ancillary services.

Deferred distribution costs - Primarily relates to the recovery of legacy meters that were replaced with smart meters. Amounts are amortized through 2020.

Contract valuations - Primarily relates to changes in the fair value of NUG contracts. See Note 8, "Derivative Instruments."

Storm-related costs - Relates to the recovery of storm costs, of which approximately $25 million and $22 million are currently being recovered through rates as of December 31, 2019 and 2018, respectively.

The following table provides information about the composition of net regulatory assets that do not earn a current return as of December 31, 2019 and 2018, all of which are currently being recovered through rates over varying periods depending on the nature of the deferral and the jurisdiction:

Regulatory Assets by Source Not Earning a Current Return	December 31, 2019	December 31, 2018	Change
Storm-related costs	$ 24	$ 19	$ 5
Regulatory transition costs	4	7	(3)
Regulatory Assets Not Earning a Current Return	$ 28	$ 26	$ 2

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment reflects original cost (net of any impairments recognized), including payroll and related costs such as taxes, employee benefits, administrative and general costs, and interest costs incurred to place the assets in service. The costs of normal maintenance, repairs and minor replacements are expensed as incurred. PN recognizes liabilities for planned major maintenance projects as they are incurred.

PN provides for depreciation on a straight-line basis at various rates over the estimated lives of property included in plant in service. Depreciation expense was approximately 2.6% of average depreciable property in 2019 and 2018.

For the year ended December 31, 2019 capitalized financing costs on PN's Consolidated Statements of Income include $2 million of allowance for equity funds used during construction and $1 million of capitalized interest. For the year ended December 31, 2018, capitalized financing costs on PN's Consolidated Statements of Income include $1 million of capitalized interest.

PN evaluates long-lived assets classified as held and used for impairment when events or changes in circumstances indicate the carrying value of the long-lived assets may not be recoverable. First, the estimated undiscounted future cash flows attributable to the assets is compared with the carrying value of the assets. If the carrying value is greater than the undiscounted future cash flows, an impairment charge is recognized equal to the amount the carrying value of the assets exceeds its estimated fair value.

INVESTMENT IN UNCONSOLIDATED AFFILIATE

Following receipt of necessary regulatory approvals, on January 31, 2017, MAIT issued membership interests to FET, PN and ME in exchange for their respective cash and transmission asset contributions. MAIT, a transmission-only subsidiary of FET, owns and operates all of the FERC-jurisdictional transmission assets previously owned by ME and PN, consisting of approximately 4,260 circuit miles of transmission lines with nominal voltages of 500 kV, 345 kV, 230 kV, 138 kV, 115 kV, 69 kV and 46 kV in the PJM Region.

PN's investment in an unconsolidated affiliate consists of a 49% ownership of MAIT, which is accounted for under the equity method of accounting.

The following is a summary of financial information for MAIT as reported in its separate financial statements:

	Year Ended December 31,	
(In millions)	2019	2018
Statements of Income Information:		
Operating revenues	$ 227	$ 154
Operating expenses	113	88
Operating income	114	66
Net income	73	54

	Year Ended December 31,	
(In millions)	2019	2018
Balance Sheet Information:		
Assets:		
Current assets	$ 28	$ 114
Property, plant and equipment, net	1,690	1,319
Deferred charges and other assets	225	225
Total assets	$ 1,943	$ 1,658
Liabilities and capitalization:		
Current liabilities	$ 298	$ 6
Long-term debt	446	446
Non-current liabilities	273	277
Total equity	926	929
Total liabilities and capitalization	$ 1,943	$ 1,658

GOODWILL

In a business combination, the excess of the purchase price over the estimated fair values of the assets acquired and liabilities assumed is recognized as goodwill. PN evaluates goodwill for impairment annually on July 31 and more frequently if indicators of impairment arise. In evaluating goodwill for impairment, PN assesses qualitative factors to determine whether it is more likely than not (that is, likelihood of more than 50%) that the fair value of a reporting unit is less than its carrying value (including goodwill). If PN concludes that it is not more likely than not that the fair value of a reporting unit is less than its carrying value, then no further testing is required. However, if PN concludes that it is more likely than not that the fair value of a reporting unit is less than its carrying value or bypasses the qualitative assessment, then the quantitative goodwill impairment test is performed to identify a potential goodwill impairment and measure the amount of impairment to be recognized, if any.

No impairment of goodwill was indicated as a result of testing in 2019 and 2018. In 2019 and 2018, PN performed a qualitative assessment, assessing economic, industry and market considerations in addition to PN's overall financial performance. It was determined that the fair value was, more likely than not, greater than its carrying value and a quantitative analysis was not necessary.

NEW ACCOUNTING PRONOUNCEMENTS

Recently Adopted Pronouncements

ASU 2016-02, *"Leases (Topic 842)*" (Issued February 2016 and subsequently updated to address implementation questions): The new guidance requires organizations that lease assets with lease terms of more than 12 months to recognize assets and liabilities for the rights and obligations created by those leases on their balance sheets as well as new qualitative and quantitative disclosures. PN implemented a third-party software tool that assisted with the initial adoption and will assist with ongoing compliance. PN chose to apply the requirements of the standard in the period of adoption (January 1, 2019) with no restatement of prior periods. Upon adoption, on January 1, 2019, PN increased assets and liabilities by $13 million, with no impact to results of operations or cash flows. See Note 6, "Leases," for additional information on PN's leases.

Recently Issued Pronouncements - The following new authoritative accounting guidance issued by the FASB has not yet been adopted. Unless otherwise indicated, PN is currently assessing the impact such guidance may have on its financial statements and disclosures, as well as the potential to early adopt where applicable. PN has assessed other FASB issuances of new standards not described below and has not included these standards based upon the current expectation that such new standards will not significantly impact PN's financing reporting.

ASU 2016-13, *"Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments"* (Issued June 2016 and subsequently updated): ASU 2016-13 removes all recognition thresholds and will require companies to recognize an allowance for credit losses for the difference between the amortized cost basis of a financial instrument and the amount of amortized cost that the company expects to collect over the instrument's contractual life. The ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019, with early adoption permitted. PN has analyzed its financial instruments within the scope of this guidance, primarily trade receivables and AFS debt securities, and does not expect a material impact to its financial statements upon adoption in 2020.

ASU 2018-15, "*Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract"* (Issued August 2018): ASU 2018-15 requires implementation costs incurred by customers in cloud computing arrangements to be deferred and recognized over the term of the arrangement, if those costs would be capitalized by the customers in a software licensing arrangement. The guidance will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019, with early adoption permitted. PN does not expect a material impact to its financial statements upon adoption in 2020.

ASU 2019-12, *"Simplifying the Accounting for Income Taxes"* (Issued in December 2019): ASU 2019-12 enhances and simplifies various aspects of the income tax accounting guidance including the elimination of certain exceptions related to the approach for intraperiod tax allocation, the methodology for calculating income taxes in an interim period and the recognition of deferred tax liabilities for outside basis differences. The new guidance also simplifies aspects of the accounting for franchise taxes and enacted changes in tax laws or rates and clarifies the accounting for transactions that result in a step-up in the tax basis of goodwill. The guidance will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020, with early adoption permitted.

2. REVENUE

PN accounts for revenues from contracts with customers under ASC 606, "*Revenue from Contracts with Customers*." Revenue from leases, financial instruments, other contractual rights or obligations and other revenues that are not from contracts with customers are outside the scope of the new standard and accounted for under other existing GAAP. PN has elected to exclude sales taxes and other similar taxes collected on behalf of third parties from revenue as prescribed in the new standard. As a result, tax collections and remittances within the scope of this election are excluded from recognition in the income statement and instead recorded through the balance sheet. Gross receipts taxes that are assessed on PN are not subject to the election and are included in revenue. PN has elected the optional invoice practical expedient for most of its revenues, which eliminates the need to provide certain revenue disclosures regarding unsatisfied performance obligations.

PN's principal business is providing electric service to customers in Pennsylvania. PN's distribution customers are metered on a cycle basis. An estimate of unbilled revenues is calculated to recognize electric service provided from the last meter reading through the end of the month. This estimate includes many factors, among which are historical customer usage, load profiles, estimated weather impacts and prices in effect for each class of customer. In each accounting period, PN accrues the estimated unbilled amount as revenue and reverses the related prior period estimate. Customer payments are generally due within 30 days. Retail generation sales relate to generation sales in Pennsylvania that are regulated by the PPUC.

PN earns revenue from state-regulated rate tariffs under which it provides **distribution services** to residential, commercial and industrial customers in its service territory. PN is obligated under the regulated construct to deliver power to customers reliably, as it is needed, which creates an implied monthly contract with the end-use customer. See Note 12, "Regulatory Matters," for additional information on rate recovery mechanisms. Distribution revenues are recognized over time as electricity is distributed and delivered to the customer and the customers consume the electricity immediately as delivery occurs.

Retail generation sales relate to SOS requirements in Pennsylvania. PN has default service obligations to provide power to non-shopping customers who have elected to continue to receive service under regulated retail tariffs. The volume of these sales varies depending on the level of shopping that occurs. Supply plans vary by state and by service territory. Default service for PN are provided through a competitive procurement process approved by the state commission. Retail generation revenues are recognized over time as electricity is delivered and consumed immediately by the customer.

Wholesale sales primarily consist of generation and capacity sales into the PJM market from NUGs. PN may also purchase power from PJM to supply power to their customers. Generally, these power sales from generation and purchases to serve load are netted hourly and reported gross as either revenues or purchased power on the Consolidated Statements of Income (Loss) based on whether the entity was a net seller or buyer each hour. Capacity revenues are recognized ratably over the PJM planning year at prices cleared in the annual BRA and incremental auctions. Capacity purchases and sales through PJM capacity auctions are reported within revenues on the Consolidated Statements of Income (Loss). Certain capacity income (bonuses) and charges (penalties) related to the availability of units that have cleared in the auctions are unknown and not recorded in revenue until, and unless, they occur.

The following table represents a disaggregation of revenue from contracts with customers for the years ended December 31, 2019 and 2018, by type of service:

Revenues by Type of Service	For the Year Ended December 31, 2019	2018
	(In millions)	
Distribution services	$ 550	$ 538
Retail generation	286	325
Wholesale sales	25	33
Other	12	11
Total revenues from contracts with customers (1)	873	907
Other non-customer revenue	8	8
Total Revenues	$ 881	$ 915

(1) Includes $12 million in reductions to revenue related to amounts subject to refund resulting from the Tax Act for the year ended December 31, 2018. Amounts were immaterial for the year ended December 31, 2019.

Other revenue includes revenue from pole attachments of $8 million and $4 million associated with late payment charges for the years ended December 31, 2019 and 2018.

The following table represents a disaggregation of PN's revenue from contracts with distribution service and retail generation customers for the years ended December 31, 2019 and 2018, by class:

Revenues by Customer Class	For the Years Ended December 31, 2019	2018
	(In millions)	
Residential	$ 564	$ 581
Commercial	152	184
Industrial	113	90
Other	7	8
Total Revenues	$ 836	$ 863

3. ACCUMULATED OTHER COMPREHENSIVE INCOME

The changes in AOCI for the years ended December 31, 2019 and 2018 for PN are shown in the following table:

	Defined Benefit Pension & OPEB Plans
	(In millions)
AOCI Balance, January 1, 2018	$ 6
Amounts reclassified from AOCI	(4)
Other comprehensive income	(4)
Income tax benefits on other comprehensive income	(3)
Other comprehensive loss, net of tax	(1)
AOCI Balance, December 31, 2018	$ 5
Amounts reclassified from AOCI	(2)
Other comprehensive loss	(2)
Income tax benefits on other comprehensive loss	(1)
Other comprehensive loss, net of tax	(1)
AOCI Balance, December 31, 2019	$ 4

The following amounts were reclassified from AOCI for PN in the years ended December 31, 2019 and 2018:

Reclassifications out of AOCI [(1)]	**For the Years Ended December 31,** 2019	**2018** [(2)]	**Affected Line Item in the Consolidated Statements of Net Income**
	(In millions)		
Defined Benefit Pension and OPEB Plans			
Prior-service costs	$ (2)	$ (4) [(3)]	
	1	3	Income taxes
	$ (1)	$ (1)	Net of tax

(1) Amounts in parenthesis represent credits to the Consolidated Statements of Income from AOCI.

(2) Includes stranded tax amounts reclassified from AOCI in connection with the adoption of ASU 2018-02, "*Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*."

(3) These AOCI components are included in the computation of net periodic pension cost. See Note 4, "Pension and Other Postemployment Benefits," for additional details.

4. PENSION AND OTHER POSTEMPLOYMENT BENEFITS

FirstEnergy provides noncontributory qualified defined benefit pension plans that cover substantially all of its employees and non-qualified pension plans that cover certain employees, including employees of PN. The plans provide defined benefits based on years of service and compensation levels. Under the cash-balance portion of the Pension Plan (for employees hired on or after January 1, 2014), FirstEnergy makes contributions to eligible employee retirement accounts based on a pay credit and an interest credit. In addition, FirstEnergy provides a minimum amount of noncontributory life insurance to retired employees in addition to optional contributory insurance. Health care benefits, which include certain employee contributions, deductibles and co-payments, are also available upon retirement to certain employees, their dependents and, under certain circumstances, their survivors. PN recognizes its allocated portion of the expected cost of providing pension and OPEB to employees and their beneficiaries and covered dependents from the time employees are hired until they become eligible to receive those benefits. PN also recognizes its allocated portion of obligations to former or inactive employees after employment, but before retirement, for disability-related benefits.

FirstEnergy recognizes a pension and OPEB mark-to-market adjustment for the change in the fair value of plan assets and net actuarial gains and losses annually in the fourth quarter of each fiscal year and whenever a plan is determined to qualify for a remeasurement. The remaining components of pension and OPEB expense, primarily service costs, interest on obligations, assumed return on assets and prior service costs, are recorded on a monthly basis. In 2019, the pension and OPEB mark-to-market adjustment primarily reflects a 110 bps decrease in the discount rate used to measure benefit obligations and higher than expected asset returns. PN's pension and OPEB mark-to-market adjustments for the years ended December 31, 2019 and 2018, were $41 million and $3 million, respectively.

FirstEnergy's pension and OPEB funding policy is based on actuarial computations using the projected unit credit method. In January 2018, FirstEnergy satisfied its minimum required funding obligations to its qualified pension plan of $500 million and addressed anticipated required funding obligations through 2020 to its pension plan with an additional contribution of $750 million ($65 million at PN). On February 1, 2019, FirstEnergy made a $500 million voluntary cash contribution to the qualified pension plan ($1 million at PN). FirstEnergy expects no required contributions through 2021.

Pension and OPEB costs are affected by employee demographics (including age, compensation levels and employment periods), the level of contributions made to the plans and earnings on plan assets. Pension and OPEB costs may also be affected by changes in key assumptions, including anticipated rates of return on plan assets, the discount rates and health care trend rates used in determining the projected benefit obligations for pension and OPEB costs. FirstEnergy uses a December 31 measurement date for its pension and OPEB plans. The fair value of the plan assets represents the actual market value as of the measurement date.

FirstEnergy's assumed rate of return on pension plan assets considers historical market returns and economic forecasts for the types of investments held by the pension trusts. In 2019, FirstEnergy's pension and OPEB plan assets experienced gains of $1,492 million, or 20.2%, compared to losses of $371 million, or (4.0)%, in 2018, and assumed a 7.5% rate of return for 2019 and 2018 which generated $569 million and $605 million of expected returns on plan assets, respectively. The expected return on pension and OPEB assets is based on the trusts' asset allocation targets and the historical performance of risk-based and fixed income securities. The gains or losses generated as a result of the difference between expected and actual returns on plan assets will decrease or increase future net periodic pension and OPEB cost as the difference is recognized annually in the fourth quarter of each fiscal year or whenever a plan is determined to qualify for remeasurement.

During 2019, the Society of Actuaries published new mortality tables that include more current data than the RP-2014 tables as well as new improvement scales. An analysis of FirstEnergy pension and OPEB plan mortality data indicated the use of the Pri-2012 mortality table with projection scale MP-2019 was most appropriate. As such, the Pri-2012 mortality table with projection scale MP-2019 was utilized to determine the 2019 benefit cost and obligation as of December 31, 2019 for the FirstEnergy pension and

OPEB plans. The impact of using the Pri-2012 mortality table with projection scale MP-2019 resulted in a decrease to the projected benefit obligation approximately $29 million and $3 million for the pension and OPEB plans, respectively, and was included in the 2019 pension and OPEB mark-to-market adjustment.

Effective in 2019, FirstEnergy changed the approach utilized to estimate the service cost and interest cost components of net periodic benefit cost for pension and OPEB plans. Historically, FirstEnergy estimated these components utilizing a single, weighted average discount rate derived from the yield curve used to measure the benefit obligation. FirstEnergy has elected to use a spot rate approach in the estimation of the components of benefit cost by applying specific spot rates along the full yield curve to the relevant projected cash flows, as this provides a better estimate of service and interest costs by improving the correlation between projected benefit cash flows to the corresponding spot yield curve rates. This election is considered a change in estimate and, accordingly, accounted for prospectively, and did not have a material impact on FirstEnergy's financial statements.

Following adoption of ASU 2017-07, "*Compensation-Retirement Benefits: Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*" in 2018, service costs, net of capitalization, continue to be reported within Other operating expenses on the PN Consolidated Statements of Income. Non-service costs are reported within Miscellaneous income, net, within Other Income (Expense).

The following is a summary of the plan status:

	Pension		OPEB	
For the years ended	**2019**	**2018**	**2019**	**2018**
	(In millions)			
FirstEnergy benefit obligation	$ 11,050	$ 9,462	$ 654	$ 608
FirstEnergy fair value of plan assets	8,395	6,984	458	408
FirstEnergy funded status	(2,655)	(2,478)	(196)	(200)
FirstEnergy accumulated benefit obligation	10,439	8,951	—	—
FirstEnergy net periodic costs (credits) (1)	703	287	(20)	(156)
PN's share of net periodic costs (credits) (1)	21	14	(2)	(25)
PN's share of net liability (2)	72	55	91	92

(1) Includes annual pension and OPEB mark-to-market adjustment.
(2) Excludes $136 million and $116 million as of December 31, 2019 and 2018, respectively, of affiliated non-current liabilities related to pension and OPEB mark-to-market costs allocated to PN.

	Pension		OPEB	
	2019	**2018**	**2019**	**2018**
Assumptions Used to Determine Benefit Obligations				
(as of December 31)				
Discount rate	3.34%	4.44%	3.18%	4.30%
Rate of compensation increase	4.10%	4.10%	N/A	N/A
Cash balance weighted average interest crediting rate	2.57%	3.34%	N/A	N/A
Assumed Health Care Cost Trend Rates				
(as of December 31)				
Health care cost trend rate assumed (pre/post-Medicare)	N/A	N/A	6.0-5.5%	6.0-5.5%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	N/A	N/A	4.5%	4.5%
Year that the rate reaches the ultimate trend rate	N/A	N/A	2028	2028
Assumptions Used to Determine Net Periodic Benefit Cost*				
for Years Ended December 31				
Weighted-average discount rate	4.44%	3.75%	4.30%	3.50%
Expected long-term return on plan assets	7.50%	7.50%	7.50%	7.50%
Rate of compensation increase	4.10%	4.20%	N/A	N/A

*Excludes impact of pension and OPEB mark-to-market adjustment.

In selecting an assumed discount rate, FirstEnergy considers currently available rates of return on high-quality fixed income investments expected to be available during the period to maturity of the pension and OPEB obligations. The assumed rates of return on plan assets consider historical market returns and economic forecasts for the types of investments held by FirstEnergy's pension trusts. The long-term rate of return is developed considering the portfolio's asset allocation strategy.

5. TAXES

PN records income taxes in accordance with the liability method of accounting. Deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts recognized for tax purposes. Investment tax credits, which were deferred when utilized, are being amortized over the recovery period of the related property. Deferred income tax liabilities related to temporary tax and accounting basis differences and tax credit carryforward items are recognized at the statutory income tax rates in effect when the liabilities are expected to be paid. Deferred tax assets are recognized based on income tax rates expected to be in effect when they are settled.

PN is party to an intercompany income tax allocation agreement with FE that provides for the allocation of consolidated tax liabilities. Net tax benefits attributable to FirstEnergy, excluding any tax benefits derived from interest expense associated with acquisition indebtedness from the merger with GPU, are reallocated to the subsidiaries of FirstEnergy that have taxable income. That allocation is accounted for as a capital contribution to the company receiving the tax benefit.

	For the Years Ended December 31,	
INCOME TAXES:	**2019**	**2018**
	(In millions)	
Currently payable		
Federal	$ 15	$ 12
State	5	2
	20	14
Deferred, net-		
Federal	6	19
State	1	7
	7	26
Total income taxes	$ 27	$ 40

PN's tax rates are affected by permanent items, such as AFUDC equity and other flow-through items, as well as discrete items that may occur in any given period, but are not consistent from period to period. The following table provides a reconciliation of federal income tax expense at the federal statutory rate to the total income taxes for the years ended December 31, 2019 and 2018:

	For the Years Ended December 31,	
(In millions)	**2019**	**2018**
Book income before income taxes	$ 175	$ 212
Federal income tax expense at statutory rate	37	45
Increases (reductions) in taxes resulting from-		
State income taxes, net of federal tax benefit	11	14
AFUDC equity and other flow-through	(7)	(6)
Equity in earnings of affiliates	(7)	(6)
Excess deferred tax amortization due to the Tax Act	(7)	(6)
Other, net	—	(1)
Total income taxes	$ 27	$ 40
Effective income tax rate	15.4%	18.9%

PN's effective tax rate on pre-tax income in 2019 and 2018 was 15.4% and 18.9%, respectively. The decrease in the effective tax rate is primarily due to increases in the tax benefits associated with state flow-through and the amortization of net excess deferred income taxes as compared to 2018 (See Note 12, "Regulatory Matters" for additional detail).

Accumulated deferred income taxes as of December 31, 2019 and 2018 are as follows:

	As of December 31,	
(In millions)	2019	2018
Property basis differences	$ 463	$ 439
Regulatory asset/liability	3	10
NUG costs	(14)	(21)
Pension and OPEB	(87)	(75)
Nuclear decommissioning activities	39	37
Loss carryforwards	(64)	(70)
Asset retirement obligations	(51)	(48)
Other	12	5
Net deferred income tax liabilities	$ 301	$ 277

PN has recorded as deferred income tax assets the effect of NOLs and tax credits that will more likely than not be realized through future operations and through the reversal of existing temporary differences. As of December 31, 2019, PN's loss carryforwards consisted of approximately $102 million ($22 million, net of tax) of Federal NOL carryforwards that begin to expire in 2031 and $524 million ($41 million, net of tax) of state NOL carryforwards that will begin to expire in 2021.

PN accounts for uncertainty in income taxes recognized in its financial statements. A recognition threshold and measurement attribute are utilized for financial statement recognition and measurement of tax positions taken or expected to be taken on a company's tax return. In 2018, PN reversed all previously recorded unrecognized tax benefits of approximately $8 million, none of which impacted PN’s effective tax rate, and did not record any new reserves in 2019. For the years ended December 31, 2019 and 2018, PN does not have a reserve for any uncertain tax positions.

PN recognizes interest expense or income and penalties related to uncertain tax positions in income taxes. That amount is computed by applying the applicable statutory interest rate to the difference between the tax position recognized and the amount previously taken or expected to be taken on the tax return. During 2019, PN did not record any interest related to uncertain tax positions, and in 2018 PN's recognition of net interest associated with unrecognized tax benefits was not material. For the years ended December 31, 2019 and 2018, PN does not have any cumulative net interest payable on its balance sheet.

For federal income tax purposes, PN files as a member of the FE consolidated group. In June 2019, the IRS completed its examination of FirstEnergy's 2017 federal income tax return and issued a Full Acceptance Letter with no changes or adjustments to PN's taxable income. Tax year 2018 is currently under review by the IRS. PN has tax returns under review by state taxing authorities at the audit or appeals level for tax years 2009 and 2013-2018.

General Taxes

Details of general taxes for the years ended 2019 and 2018 are shown below:

(In millions)	2019	2018
Gross receipts	$ 49	$ 49
Real and personal property	2	1
Social security and unemployment	6	7
Other	—	1
Total general taxes	$ 57	$ 58

6. LEASES

PN primarily leases vehicles as well as building space, land, and other property and equipment under cancelable and noncancelable leases.

In addition, MAIT has a ground lease with PN under an operating lease agreement. PN reserves the right to use (and to permit authorized others to use) the land for any purpose that does not cause a violation of electrical safety code or applicable law, or does not impair MAIT's ability to satisfy its service obligations. Additional uses of such land for MAIT's facilities requires prior written approval from the applicable operating company. MAIT purchases directly any new property acquired for transmission use. MAIT makes variable quarterly lease payments through January 1, 2043, unless terminated prior to maturity, or extended by MAIT for up to two additional successive periods of 25 years each and one successive term of 24 years. Revenue associated with this agreement was approximately $1 million in 2019 and 2018.

PN adopted ASU 2016-02, *"Leases (Topic 842)*" on January 1, 2019, and elected a number of transitional practical expedients provided within the standard. These included a "package of three" expedients that must be taken together and allowed entities to (1) not reassess whether existing contracts contain leases, (2) carryforward the existing lease classification, and (3) not reassess initial direct costs associated with existing leases. In addition, PN elected the option to apply the requirements of the standard in the period of adoption (January 1, 2019) with no restatement of prior periods. Adoption of the standard on January 1, 2019, did not result in a material cumulative effect adjustment upon adoption. PN did not evaluate land easements under the new guidance as they were not previously accounted for as leases. PN also elected not to separate lease components from non-lease components as non-lease components were not material.

Leases with an initial term of 12 months or less are recognized as lease expense on a straight-line basis over the lease term and not recorded on the balance sheet. Most leases include one or more, options to renew and certain leases include options to terminate. The exercise of lease renewal options is at PN's sole discretion. Renewal options are included within the lease liability if they are reasonably certain based on various factors relative to the contract. Certain leases also include options to purchase the leased property. The depreciable life of leased assets and leasehold improvements are limited by the expected lease term, unless there is a transfer of title or purchase option reasonably certain of exercise.

For vehicles leased under master 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. As of December 31, 2019, the maximum potential loss for these lease agreements at the end of the lease term is approximately $1 million.

Finance leases for assets used in regulated operations are recognized in PN's Statement of Income such that amortization of the right-of-use asset and interest on lease liabilities equals the expense allowed for ratemaking purposes. All operating lease expenses are recognized in Other operating expense.

The components of lease expense for the year ended December 31, 2019, were as follows:

(In millions)		
Operating lease costs [1]	$	3
Finance lease costs:		
Amortization of right-of-use assets		3
Interest on lease liabilities		1
Total finance lease cost		4
Total lease cost	$	7

[1] Includes $1 million of short-term lease costs.

Supplemental cash flow information related to leases was as follows:

(In millions)	For the Year Ended December 31, 2019	
Cash paid for amounts included in the measurement of lease liabilities		
Operating cash flows from operating leases	$	3
Operating cash flows from finance leases		—
Finance cash flows from finance leases		3
Right-of-use assets obtained in exchange for lease obligations:		
Operating leases	$	11
Finance leases		—

Supplemental balance sheet information related to leases was as follows:

(In millions)	Financial Statement Line Item	As of December 31, 2019	
Assets			
Operating lease assets, net of accumulated amortization of $2 million	Deferred charges and other assets	$	22
Finance lease assets, net of accumulated amortization of $21 million	Property, plant and equipment		10
Total leased assets		$	32
Liabilities			
Current:			
Operating	Other current liabilities	$	3
Finance	Currently payable long-term debt		4
Noncurrent:			
Operating	Other noncurrent liabilities		18
Finance	Long-term debt and other long-term obligations		6
Total leased liabilities		$	31

Lease terms and discount rates were as follows:

	As of December 31, 2019
Weighted-average remaining lease terms (years)	
Operating leases	7.27
Finance leases	3.28
Weighted-average discount rate (1)	
Operating leases	3.24%
Finance leases	3.44%

(1) When an implicit rate is not readily determinable, an incremental borrowing rate is utilized, determining the present value of lease payments. The rate is determined based on expected term and information available at the commencement date.

Maturities of lease liabilities as of December 31, 2019, were as follows:

(In millions)	Operating Leases	Finance Leases	Total
2020	$ 4	$ 4	$ 8
2021	3	3	6
2022	3	2	5
2023	3	1	4
2024	3	—	3
Thereafter	8	—	8
Total lease payments	24	10	34
Less imputed interest	(3)	—	(3)
Total net present value	$ 21	$ 10	$ 31

As of December 31, 2019, additional operating leases agreements, primarily for vehicles, that have not yet commenced are $2 million. These leases are expected to commence within the next 18 months with lease terms of 5 to 10 years.

ASC 840, "Leases" Disclosures

PN's estimated future minimum lease payments for capital and operating leases as of December 31, 2018, as reported in the 2018 financial statements under ASC 840, with initial or remaining lease terms in excess of one year are as follows:

(In millions)	2019	2020	2021	2022	2023	Thereafter	Total	Less: amount representing interest and fees	Present value of net minimum capital lease payments
Capital leases	$ 4	$ 4	$ 3	$ 2	$ 1	$ —	$ 14	$ 1	$ 13
Operating leases	$ 3	$ 2	$ 2	$ 2	$ 2	$ 6	$ 17	N/A	N/A

Operating lease expense under ASC 840 "*Leases*" for the year ended December 31, 2018 was $3 million.

7. FAIR VALUE MEASUREMENTS

RECURRING FAIR VALUE MEASUREMENTS

Authoritative accounting guidance establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy gives the highest priority to Level 1 measurements and the lowest priority to Level 3 measurements. The three levels of the fair value hierarchy and a description of the valuation techniques are as follows:

Level 1 - Quoted prices for identical instruments in active markets.

Level 2 - Quoted prices for similar instruments in active markets;
- Quoted prices for identical or similar instruments in markets that are not active;
- Model-derived valuations for which all significant inputs are observable market data.

Models are primarily industry-standard models that consider various assumptions, including quoted forward prices for commodities, time value, volatility factors and current market and contractual prices for the underlying instruments, as well as other relevant economic measures.

Level 3 - Valuation inputs are unobservable and significant to the fair value measurement.

FirstEnergy produces a long-term power and capacity price forecast annually with periodic updates as market conditions change. When underlying prices are not observable, prices from the long-term price forecast (see Note 8, "Derivative Instruments"), are used to measure fair value. A more detailed description of PN's valuation process for NUG contracts follows:

NUG contracts represent purchased power agreements with third-party non-utility generators that are transacted to satisfy certain obligations under PURPA. NUG contract carrying values are recorded at fair value and adjusted periodically using a mark-to-model methodology, which approximates market. The primary unobservable inputs into the model are regional power prices and generation MWH. Pricing for the NUG contracts is a combination of market prices for the current year and next two years based on observable data and internal models using historical trends and market data for the remaining years under contract. The internal models use forecasted energy purchase prices as an input when prices are not defined by the contract. Forecasted market prices are based on ICE quotes and management assumptions. Generation MWH reflects data provided by contractual arrangements and historical trends. The model calculates the fair value by multiplying the prices by the generation MWH. Significant increases or decreases in inputs in isolation may have resulted in a higher or lower fair value measurement.

PN primarily applies the market approach for recurring fair value measurements using the best information available. Accordingly, PN maximizes the use of observable inputs and minimizes the use of unobservable inputs. There were no changes in valuation methodologies used as of December 31, 2019 from those used as of December 31, 2018. The determination of the fair value measures takes into consideration various factors, including but not limited to, nonperformance risk, counterparty credit risk and the impact of credit enhancements (such as cash deposits, letters of credit and priority interests). The impact of these forms of risk was not significant to the fair value measurements.

The following tables set forth the recurring assets and liabilities that are accounted for at fair value by level within the fair value hierarchy:

Recurring Fair Value Measurements	**December 31, 2019**				**December 31, 2018**			
	Level 1	**Level 2**	**Level 3**	**Total**	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets				***(In millions)***				
Corporate debt securities	$ —	$ 26	$ —	$ 26	$ —	$ 90	$ —	$ 90
Equity securities[(1)]	—	—	—	—	92	—	—	92
Foreign government debt securities	—	—	—	—	—	3	—	3
U.S. government debt securities	—	—	—	—	—	5	—	5
Other[(2)]	—	196	—	196	—	4	—	4
Total assets	—	222	—	222	92	102	—	194
Liabilities								
Derivative liabilities - NUG contracts[(3)]	—	—	(16)	(16)	—	—	(43)	(43)
Total liabilities	—	—	(16)	(16)	—	—	(43)	(43)
Net assets (liabilities)[(4)]	$ —	$ 222	$ (16)	$ 206	$ 92	$ 102	$ (43)	$ 151

(1) NDT funds hold equity portfolios whose performance is benchmarked against the Alerian MLP Index.
(2) Primarily consists of short-term cash investments.
(3) NUG contracts are subject to regulatory accounting treatment and changes in market value do not impact earnings.
(4) Excludes $(8) million and $(3) million as of December 31, 2019 and December 31, 2018, respectively, of receivables, payables, taxes and accrued income associated with financial instruments reflected within the fair value table.

The following table provides a reconciliation of changes in the fair value of NUGs held by PN and classified as Level 3 in the fair value hierarchy for the periods ended December 31, 2019 and December 31, 2018:

(In millions)	**Net Derivative Liability NUG Contracts**[(1)]
Balance, January 1, 2018	$ (79)
Unrealized gain	2
Settlements	34
Balance, December 31, 2018	(43)
Unrealized loss	(12)
Settlements	39
Balance, December 31, 2019	$ (16)

(1) NUG contracts are subject to regulatory accounting treatment and changes in market value do not impact earnings.

Level 3 Quantitative Information

The following table provides quantitative information for NUG contracts that are classified as Level 3 in the fair value hierarchy for the period ended December 31, 2019:

	Fair Value, Net *(In millions)*		Valuation Technique	Significant Input	Range	Weighted Average	Units
				Generation	400 to 330,000	115,000	MWH
NUG Contracts	$	(16)	Model	Regional electricity prices	$25.30 to $35.20	$26.30	Dollars/MWH

INVESTMENTS

All temporary cash investments purchased with an initial maturity of three months or less are reported as cash equivalents on the Consolidated Balance Sheets at cost, which approximates their fair market value. Investments other than cash and cash equivalents include equity securities, AFS debt securities and other investments. PN has no debt securities held for trading purposes.

Generally, unrealized gains and losses on equity securities are recognized in income whereas unrealized gains and losses on AFS debt securities are recognized in AOCI. However, the NDTs of PN are subject to regulatory accounting with all gains and losses on equity and AFS debt securities offset against regulatory assets.

The investment policy for the NDT funds restricts or limits the trusts' ability to hold certain types of assets including private or direct placements, warrants, securities of FirstEnergy, investments in companies owning nuclear power plants, financial derivatives, securities convertible into common stock and securities of the trust funds' custodian or managers and their parents or subsidiaries.

AFS Securities

PN holds debt and equity securities within the NDT trusts. These trust investments are considered AFS securities and recognized at fair market value. As further discussed in Note 13, "Commitments and Contingencies," assets and liabilities held for sale on the PN Consolidated Balance Sheets associated with the TMI-2 transaction consist of an asset retirement obligation of $172 million and NDT's of $215 million.

The following table summarizes the amortized cost basis, unrealized gains, unrealized losses and fair values of investments held in NDT trusts as of December 31, 2019 and December 31, 2018.

	December 31, 2019[(1)]								December 31, 2018[(2)]							
	Cost Basis		Unrealized Gains		Unrealized Losses		Fair Value[(3)]		Cost Basis		Unrealized Gains		Unrealized Losses		Fair Value	
	(In millions)															
Debt securities	$	26	$	1	$	—	$	27	$	100	$	—	$	(3)	$	97
Equity securities	$	—	$	—	$	—	$	—	$	91	$	5	$	(4)	$	92

(1) Excludes short-term cash investments of $188 million, all of which is classified as held for sale.
(2) Excludes short-term cash investments of $2 million.
(3) Includes $27 million classified as held for sale.

Proceeds from the sale of investments in AFS securities, realized gains and losses on those sales and interest and dividend income for the years ended December 31, 2019 and 2018 were as follows.

	Sale Proceeds		Realized Gains		Realized Losses		Interest and Dividend Income	
	(In millions)							
2019	$	366	$	28	$	(7)	$	7
2018	$	154	$	8	$	(9)	$	7

LONG-TERM DEBT AND OTHER LONG-TERM OBLIGATIONS

All borrowings with initial maturities of less than one year are defined as short-term financial instruments under GAAP and are reported as Short-term borrowings on the Consolidated Balance Sheets at cost. Since these borrowings are short-term in nature, PN believes that their costs approximate their fair market value. The following table provides the approximate fair value and related carrying amounts of long-term debt, which excludes finance lease obligations and net unamortized debt issuance costs and discounts:

	December 31, 2019		December 31, 2018	
(In millions)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt	$ 1,300	$ 1,395	$ 1,125	$ 1,161

The fair values of long-term debt and other long-term obligations reflect the present value of the cash outflows relating to those securities based on the current call price, the yield to maturity or the yield to call, as deemed appropriate at the end of each respective period. The yields assumed were based on securities with similar characteristics offered by corporations with credit ratings similar to those of PN. PN classified short-term borrowings, long-term debt and other long-term obligations as Level 2 in the fair value hierarchy as of December 31, 2019 and December 31, 2018.

8. DERIVATIVE INSTRUMENTS

PN is exposed to financial risks resulting from fluctuating interest rates and commodity prices, including prices for electricity, coal and energy transmission. To manage the volatility related to these exposures, FirstEnergy's Risk Policy Committee, comprised of senior management, provides general management oversight for risk management activities throughout FirstEnergy, including PN. The Risk Policy Committee is responsible for promoting the effective design and implementation of sound risk management programs and oversees compliance with corporate risk management policies and established risk management practice.

NUG contracts are reflected on the Balance Sheets at fair value on a gross basis with changes in fair value recorded as regulatory assets and liabilities. PN performs qualitative analyses to determine whether a variable interest gives PN a controlling financial interest in a VIE. This analysis identifies the primary beneficiary of a VIE as the enterprise that has both the power to direct the activities of a VIE that most significantly impact the entity's economic performance and the obligation to absorb losses of the entity that could potentially be significant to the VIE or the right to receive benefits from the entity that could potentially be significant to the VIE. None of the NUG contracts qualify as a VIE.

None of the derivative instruments have been designated in a hedging relationship and none of the counterparties to these contracts require collateral to mitigate credit exposure. The portfolio of derivative instruments does not allow for the offsetting of derivative assets and derivative liabilities. The following table summarizes the fair value and classification of derivative instruments on PN's Consolidated Balance Sheets:

Derivative Liabilities

	Fair Value	
	December 31, 2019	December 31, 2018
	(In millions)	
Noncurrent Liabilities - Power Purchase Contract Liability		
NUGs	$ (16)	$ (44)

PN is expected to purchase less than 1 million MWHs of total power associated with its NUG contracts in future periods.

9. CAPITALIZATION

COMMON STOCK

In addition to paying dividends from retained earnings, PN has authorization from the FERC to pay cash dividends to FirstEnergy from paid-in capital accounts, as long as its FERC-defined equity-to-total-capitalization ratio remains above 35%.

PREFERRED STOCK

PN is authorized to issue 11,435,000 shares preferred stock, no par value, as of December 31, 2019. As of December 31, 2019, and 2018, there were no preferred shares outstanding.

LONG-TERM DEBT AND OTHER LONG-TERM OBLIGATIONS

The following table presents outstanding long-term debt and finance lease obligations for PN as of December 31, 2019 and 2018:

	As of December 31, 2019		As of December 31,	
(Dollar amounts in millions)	**Maturity Date**	**Interest Rate**	**2019**	**2018**
Unsecured notes - fixed rate	2020 - 2038	3.25% - 6.15%	$ 1,300	$ 1,125
Finance lease obligations			10	13
Unamortized debt discounts			(2)	(1)
Unamortized debt issuance costs			(8)	(6)
Currently payable long-term debt			(253)	(128)
Total long-term debt and other long-term obligations			$ 1,047	$ 1,003

On June 3, 2019, PN issued $300 million of 3.60% senior notes due 2029. Proceeds from the issuance of the senior notes were used to refinance existing indebtedness, including amounts outstanding under the FE regulated companies' money pool incurred in connection with the repayment at maturity of PN's $125 million of 6.63% senior notes due 2019, to fund capital expenditures, and for other general corporate purposes.

The following table presents scheduled debt repayments for outstanding long-term debt, excluding finance leases and unamortized debt discounts and premiums, for the next five years as of December 31, 2019:

Year	PN
	(In millions)
2020	$ 250
2021	—
2022	—
2023	—
2024	—

Debt Covenant Default Provisions

PN has various debt covenants under certain financing arrangements, including its revolving credit facility. The most restrictive of the debt covenants relate to the nonpayment of interest and/or principal on such debt and the maintenance of certain financial ratios. The failure by PN to comply with the covenants contained in any of its financing arrangements could result in an event of default, which may have an adverse effect on PN's financial condition.

Additionally, there are cross-default provisions in certain financing arrangements of FE and its subsidiaries, including PN. These provisions generally trigger a default in the applicable financing arrangement of an entity if it or any of its significant subsidiaries default under another financing arrangement in excess of a certain principal amount, typically $100 million. Although such defaults by PN would generally cross-default FE financing arrangements containing these provisions, defaults by FE would generally not cross-default applicable PN financing arrangements.

As of December 31, 2019, PN was in compliance with all debt covenant default provisions.

10. SHORT-TERM BORROWINGS AND BANK LINES OF CREDIT

PN had no outstanding short-term borrowings as of December 31, 2019 and $50 million of outstanding short-term borrowings as of December 31, 2018.

Revolving Credit Facility

FE and the Utilities, including PN, participate in a five-year syndicated revolving credit facility providing for aggregate commitments of $2.5 billion (Facility), which are available through December 6, 2022. Under the Facility, FE and the Utilities may use borrowings under their respective facility for working capital and other general corporate purposes, including intercompany loans and advances by a borrower to any of its subsidiaries. Generally, borrowings under the Facility are available to each borrower separately and mature on the earlier of 364 days from the date of borrowing or the commitment termination date, as the same may be extended.

The Facility contains financial covenants requiring each borrower to maintain a consolidated debt-to-total-capitalization ratio (as defined under the Facility) of no more than 65% measured at the end of each fiscal quarter.

Under the Facility, PN may borrow up to its sub-limit of $300 million, all of which was available to PN as of December 31, 2019. PN has regulatory and other short-term debt limitations of $300 million which includes amounts that may be borrowed under the regulated companies' money pool.

The Facility does not contain provisions that restrict the ability to borrow or accelerate payment of outstanding advances in the event of any change in credit ratings of the borrowers. Pricing is defined in “pricing grids,” whereby the cost of funds borrowed under the Facility is related to the credit ratings of the company borrowing the funds. Additionally, borrowings under the Facility are subject to the usual and customary provisions for acceleration upon the occurrence of events of default, including a cross-default for other indebtedness in excess of $100 million.

FirstEnergy Money Pool

FE’s utility and transmission operating subsidiary companies, including PN, also have the ability to borrow from each other and the holding company to meet their short-term working capital requirements. FESC administers this money pool and tracks surplus funds of FE and the respective regulated subsidiaries, as well as proceeds available from bank borrowings. Companies receiving a loan under the money pool agreement must repay the principal amount of the loan, together with accrued interest, within 364 days of borrowing the funds. The rate of interest is the same for each company receiving a loan from the regulated pool and is based on the average cost of funds available through the pool. The average interest rate for borrowings in 2019 was 2.27% per annum.

11. ASSET RETIREMENT OBLIGATIONS

PN has recognized applicable legal obligations for AROs and its associated cost primarily for decommissioning of the TMI-2 nuclear generating facility. PN uses an expected cash flow approach to measure the fair value of its nuclear decommissioning AROs. In addition, PN has recognized conditional retirement obligations, primarily for asbestos remediation. See Note 13, "Commitments and Contingencies", for further discussion of TMI 2 liabilities.

Conditional retirement obligations associated with tangible long-lived assets are recognized at fair value in the period in which they are incurred if a reasonable estimate can be made, even though there may be uncertainty about timing or method of settlement. When settlement is conditional on a future event occurring, it is reflected in the measurement of the liability, not in the recognition of the liability.

The following table summarizes the changes to PN's ARO balances during 2019 and 2018:

ARO Reconciliation	***(In millions)***
Balance, January 1, 2018	$ 116
Changes in timing and amount of estimated cash flows	44
Accretion	7
Balance, December 31, 2018	167
Accretion	9
Balance, December 31, 2019 [(1)]	$ 176

[(1)] Includes $172 million related to TMI-2 classified as held for sale. See Note 13, "Commitments and Contingencies" for further information.

During the fourth quarter of 2018, based on studies completed by a third-party to reassess the estimated costs and timing to decommission TMI-2, PN increased their ARO by a total of approximately $44 million, which was offset against a regulatory asset. The increase in the ARO resulted primarily from accelerated timing of the estimated cash flows associated with decommissioning.

12. REGULATORY MATTERS

STATE REGULATION

PN's retail rates, conditions of service, issuance of securities and other matters are subject to regulation in Pennsylvania by the PPUC and in New York by the NYPSC. The key terms of PN's current rate orders for distribution customer billings, which have been effective since January 2017, include an allowed debt/equity ratio of 47.4%/52.6% (reflecting the filed debt/equity as final settlement/ orders do not specifically include capital structure). The PPUC-approved settlement agreement for such rates did not disclose ROE.

PENNSYLVANIA

The Pennsylvania Companies operate under rates approved by the PPUC, effective as of January 27, 2017. These rates were adjusted for the net impact of the Tax Act, effective March 15, 2018. The net impact of the Tax Act for the period January 1, 2018 through March 14, 2018 must also be separately tracked for treatment in a future rate proceeding. The Pennsylvania Companies operate under DSPs for the June 1, 2019 through May 31, 2023 delivery period, which provide for the competitive procurement of generation supply for customers who do not choose an alternative EGS or for customers of alternative EGSs that fail to provide the contracted service.

Under the 2019-2023 DSPs, supply will be provided by wholesale suppliers through a mix of 3, 12 and 24-month energy contracts, as well as two RFPs for 2-year SREC contracts for ME, PN and Penn. The 2019-2023 DSPs also include modifications to the Pennsylvania Companies’ POR programs in order to continue their clawback pilot program as a long-term, permanent program term, modifications to the Pennsylvania Companies’ customer class definitions to allow for the introduction of hourly priced default service to customers at or above 100kW, customer assistance program shopping limitations, and script modifications related to the Pennsylvania Companies' customer referral programs.

Pursuant to Pennsylvania Act 129 of 2008 and PPUC orders, Pennsylvania EDCs implement energy efficiency and peak demand reduction programs. The Pennsylvania Companies' Phase III EE&C plans for the June 2016 through May 2021 period, which were approved in March 2016, with expected costs up to $390 million, are designed to achieve the targets established in the PPUC's Phase III Final Implementation Order with full recovery through the reconcilable EE&C riders.

Pennsylvania EDCs may establish a DSIC to recover costs of infrastructure improvements and costs related to highway relocation projects with PPUC approval. LTIIPs outlining infrastructure improvement plans for PPUC review and approval must be filed prior to approval of a DSIC. The PPUC approved modified LTIIPs for ME, PN and Penn for the remaining years of 2017 through 2020 to provide additional support for reliability and infrastructure investments. Following a periodic review of the LTIIPs in 2018 as required by regulation once every five years, the PPUC entered an Order concluding that the Pennsylvania Companies have substantially adhered to the schedules and expenditures outlined in their LTIIPs, but that changes to the LTIIPs as designed are necessary to maintain and improve reliability and directed the Pennsylvania Companies to file modified or new LTIIPs. On May 23, 2019, the PPUC approved the Pennsylvania Companies’ Modified LTIIPs that revised LTIIP spending in 2019 of approximately $25 million by PN, and terminating at the end of 2019. On August 30, 2019, the Pennsylvania Companies filed Petitions for approval of proposed LTIIPs for the five-year period beginning January 1, 2020 and ending December 31, 2024 for a total capital investment of approximately $572 million for certain infrastructure improvement initiatives. On January 16, 2020, the PPUC approved the LTIIPs without modification, as well as directed the Pennsylvania Companies to submit corrective action plans by March 16, 2020, which outline how they will reduce their pole replacement backlogs over a five-year period to a rolling two-year backlog.

The Pennsylvania Companies' approved DSIC riders for quarterly cost recovery went into effect July 1, 2016, subject to hearings and refund or reallocation among customer classes. In the January 19, 2017 order approving the Pennsylvania Companies’ general rate cases, the PPUC added an additional issue to the DSIC proceeding to include whether ADIT should be included in DSIC calculations. The parties to the DSIC proceeding submitted a Joint Settlement that resolved the issues that were pending from the order issued on June 9, 2016, and the PPUC approved the Joint Settlement without modification and reversed the ALJ's previous decision that would have required the Pennsylvania Companies to reflect all federal and state income tax deductions related to DSIC-eligible property in currently effective DSIC rates. The Pennsylvania OCA filed an appeal with the Pennsylvania Commonwealth Court of the PPUC's decision, and the Pennsylvania Companies contested the appeal. The Commonwealth Court reversed the PPUC’s decision of April 19, 2018 and remanded the matter to the PPUC to require the Pennsylvania Companies to revise their tariffs and DSIC calculations to include ADIT and state income taxes. The Commonwealth Court denied Applications for Reargument in the Court’s July 11, 2019 Opinion and Order filed by the PPUC and the Pennsylvania Companies. On October 7, 2019, the PPUC and the Pennsylvania Companies filed separate Petitions for Allowance of Appeal of the Commonwealth Court’s Opinion and Order to the Pennsylvania Supreme Court.

FERC REGULATORY MATTERS

Under the FPA, FERC regulates rates for interstate wholesale sales, accounting and other matters. With respect to its wholesale services and rates, PN is subject to regulation by FERC.

FERC regulates the sale of power for resale in interstate commerce in part by granting authority to public utilities to sell wholesale power at market-based rates upon showing that the seller cannot exert market power in generation or transmission or erect barriers to entry into markets. PN has been authorized by FERC to sell wholesale power in interstate commerce at market-based rates and has a market-based rate tariff on file with FERC, although major wholesale purchases remain subject to regulation by the PPUC.

Federally-enforceable mandatory reliability standards apply to the bulk electric system and impose certain operating, record-keeping and reporting requirements on PN. NERC is the ERO designated by FERC to establish and enforce these reliability standards, although NERC has delegated day-to-day implementation and enforcement of these reliability standards to six regional entities, including RFC. All of the facilities that FirstEnergy operates, including those of PN, are located within the RFC region. FirstEnergy actively participates in the NERC and RFC stakeholder processes, and otherwise monitors and manages its companies, including PN, in response to the ongoing development, implementation and enforcement of the reliability standards implemented and enforced by RFC.

FirstEnergy, including PN, believes that it is in material compliance with all currently-effective and enforceable reliability standards. Nevertheless, in the course of operating its extensive electric utility systems and facilities, FirstEnergy, including PN, occasionally learns of isolated facts or circumstances that could be interpreted as excursions from the reliability standards. If and when such occurrences are found, FirstEnergy, including PN, develops information about the occurrence and develops a remedial response to the specific circumstances, including in appropriate cases “self-reporting” an occurrence to RFC. Moreover, it is clear that NERC, RFC and FERC will continue to refine existing reliability standards as well as to develop and adopt new reliability standards. Any inability on FirstEnergy's, including PN's part to comply with the reliability standards for its bulk electric system could result in the imposition of financial penalties, or obligations to upgrade or build electric facilities, that could have a material adverse effect on PN's financial condition, results of operations and cash flows.

13. COMMITMENTS AND CONTINGENCIES

NUCLEAR INSURANCE

PN maintains property damage insurance provided by NEIL for its interest in the retired TMI-2 nuclear facility, a permanently shut down and defueled facility. Under these arrangements, up to $150 million of coverage for decontamination costs, decommissioning costs, debris removal and repair and/or replacement of property is provided. PN pays annual premiums and is subject to retrospective premium assessments of up to approximately $0.3 million during a policy year.

PN intends to maintain insurance against nuclear risks as long as it is available. To the extent that property damage, decontamination, decommissioning, repair and replacement costs and other such costs arising from a nuclear incident at any of PN's plants exceed the policy limits of the insurance in effect with respect to that plant, to the extent a nuclear incident is determined not to be covered by PN's insurance policies, or to the extent such insurance becomes unavailable in the future, PN would remain at risk for such costs.

The Price-Anderson Act limits public liability relative to a single incident at a nuclear power plant. In connection with TMI-2, PN carries the required ANI third party liability coverage and also has coverage under a Price Anderson indemnity agreement issued by the NRC. The total available coverage in the event of a nuclear incident is $560 million, which is also the limit of public liability for any nuclear incident involving TMI-2.

ENVIRONMENTAL MATTERS

Prior to November 1999, PN owned and operated electric generation facilities in Pennsylvania. In response to federal and state deregulation initiatives, it separated its electric generation business from its transmission and distribution businesses by transferring all of its generation assets to an affiliate. However, PN retained responsibility for certain liabilities and obligations arising under environmental laws up to the date of transfer. As more fully discussed below, as an historic owner and operator of generation facilities, PN has been subject to claims alleging violations of environmental law and could have exposure for fines and penalties.

OTHER LEGAL PROCEEDINGS

Nuclear Plant Matters

Under NRC regulations, PN must ensure that adequate funds will be available to decommission its retired nuclear facility, TMI-2. As of December 31, 2019, PN had approximately $215 million invested in external trusts to be used for the decommissioning and environmental remediation of its retired TMI-2 nuclear generating facility. The values of PN's NDTs also fluctuate based on market conditions. If the values of the trusts decline by a material amount, the obligation to PN to fund the trusts may increase. Disruptions in the capital markets and their effects on particular businesses and the economy could also affect the values of the NDTs.

On October 15, 2019, JCP&L, ME, PN and GPUN executed an asset purchase and sale agreement with TMI-2 Solutions, LLC, a subsidiary of Energy*Solutions*, LLC, concerning the transfer and dismantlement of TMI-2. This transfer of TMI-2 to TMI-2 Solutions, LLC will include the transfer of: (i) the ownership and operating NRC licenses for TMI-2; (ii) the external trusts for the decommissioning and environmental remediation of TMI-2; and (iii) related liabilities of approximately $900 million as of December 31, 2019. There can be no assurance that the transfer will receive the required regulatory approvals and, even if approved, whether the conditions to the closing of the transfer will be satisfied. On November 12, 2019, JCP&L filed a Petition with the NJBPU seeking approval of the transfer and sale of JCP&L’s entire 25% interest in TMI-2 to TMI-2 Solutions, LLC. Also on November 12, 2019, JCP&L, ME, PN, GPUN and TMI-2 Solutions, LLC filed an application with the NRC seeking approval to transfer the NRC license for TMI-2 to TMI-2 Solutions, LLC. Both proceedings are ongoing. Assets and liabilities held for sale on the PN's Consolidated Balance Sheet associated with the transaction consist of asset retirement obligations of $172 million, NDTs of $215 million as well as property, plant and equipment with a net book value of zero.

Other Legal Matters

There are various lawsuits, claims (including claims for asbestos exposure) and proceedings related to PN's normal business operations pending against PN and its subsidiary. The loss or range of loss in these matters is not expected to be material to PN or its subsidiary. The other potentially material items not otherwise discussed above are described under Note 12, "Regulatory Matters."

PN accrues legal liabilities only when it concludes that it is probable that it has an obligation for such costs and can reasonably estimate the amount of such costs. In cases where PN determines that it is not probable, but reasonably possible that it has a material obligation, it discloses such obligations and the possible loss or range of loss if such estimate can be made. If it were ultimately determined that PN or its subsidiary has legal liability or are otherwise made subject to liability based on any of the matters referenced above, it could have a material adverse effect on PN's or its subsidiary's financial condition, results of operations and cash flows.

14. TRANSACTIONS WITH AFFILIATED COMPANIES

PN's operating revenues, operating expenses, miscellaneous income and interest expenses include transactions with affiliated companies. These affiliated company transactions include affiliated company power sales agreements, support service billings, interest on affiliated company notes including the money pools and other transactions.

The primary affiliated company transactions for PN during the years ended December 31, 2019 and 2018 are as follows:

	For the Years Ended December 31,	
	2019	2018
	(In millions)	
Revenues [1]	$ 3	$ 3
Expenses:		
Purchased power from FES [2]	14	30
Support services	62	68
Miscellaneous Income	3	2
Interest expense to affiliates	1	1

[1] Includes ground lease revenues from MAIT. Please see Note 6, "Leases" for additional information.
[2] PN purchases power from FES to meet a portion of its POLR and default service requirements and provide power to certain facilities.

FirstEnergy does not bill directly or allocate any of its costs to any subsidiary company. Costs are allocated from FESC, a subsidiary of FE. The majority of costs are directly billed or assigned at no more than cost. The remaining costs are for services that are provided on behalf of more than one company, or costs that cannot be precisely identified and are allocated using formulas developed by FESC. The current allocation or assignment formulas used and their bases include multiple factor formulas: each company's proportionate amount of FirstEnergy's aggregate direct payroll, number of employees, asset balances, revenues, number of customers, other factors and specific departmental charge ratios. Intercompany transactions with FirstEnergy and its other subsidiaries are generally settled under commercial terms within thirty days.

Affiliate accounts receivable and accounts payable balances relate to intercompany transactions that have not yet settled through the FirstEnergy money pool (see Note 10, "Short-Term Borrowings and Bank Lines of Credit").

PN and FirstEnergy's other subsidiaries, including FES and FENOC, are parties to an intercompany income tax allocation agreement with FE and its other subsidiaries that provides for the allocation of consolidated tax liabilities. Net tax benefits attributable to FE are generally reallocated to the subsidiaries of FirstEnergy that have taxable income. That allocation is accounted for as a capital contribution to the company receiving the tax benefit (see Note 5, "Taxes").