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**TO THE INVESTMENT COMMUNITY:<sup>1</sup>**

This letter will provide an update on a recent action by the Pennsylvania Supreme Court and on several accounting issues associated with “Pension and Other Postretirement Benefits”, “Asset Retirement Obligations”, and “Assets Pending Sale”.

**Pennsylvania Supreme Court Action**

On January 17, 2003, the Pennsylvania Supreme Court denied further appeals of the February 21, 2002, Pennsylvania Commonwealth Court’s decision related to FirstEnergy’s merger with GPU, Inc. The Commonwealth Court’s decision involved two separate proceedings consolidated and decided by the Pennsylvania Public Utility Commission in the spring of 2001. (See the investor letter dated March 25, 2002 for more details. The letter is available in the Investor Information section of FirstEnergy’s Internet homepage under “Letters to the Investment Community”.)

As a result of this action, the Commonwealth Court’s decision on several merger-related issues will stand. We believe that this will have the following impacts on FirstEnergy:

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<sup>1</sup> This letter includes forward-looking statements based on information currently available to management. Such statements are subject to certain risks and uncertainties. These statements typically contain, but are not limited to, the terms "anticipate," "expect," "believe," "estimate," and similar words. Actual results may differ materially due to a number of factors including, but not limited to, the speed and nature of regulatory approvals.

- **Merger Approval**

The Commonwealth Court had affirmed the Commission's order approving the merger between FirstEnergy and GPU. Thus, the lower court's approval of the merger stands. Certain parties had sought to overturn this decision.

- **Provider of Last Resort (POLR) Relief**

The Commonwealth Court had overturned the Commission's order allowing Metropolitan Edison (Met-Ed) and Pennsylvania Electric (Penelec) to apply Competitive Transition Charge (CTC) revenues against POLR costs in excess of the companies' fixed generation tariff; therefore, providing no basis for deferral accounting for such costs. However, we do not believe this will have any significant adverse financial impact on FirstEnergy following several actions taken in the third quarter, 2002.

In the third quarter of 2002, FirstEnergy incurred a \$56 million charge (\$0.11 per share after-tax) to create a reserve against the energy costs deferred subsequent to the merger with GPU through September 30, 2002. The remaining \$231 million of deferred energy costs (i.e., the deferred balance that existed at the time of the merger close) were also reserved through purchase accounting. As a result, there are no further adjustments required for FirstEnergy.

Also in the third quarter, Met-Ed and Penelec entered into a wholesale power transaction with their unregulated supply affiliate, FirstEnergy Solutions (FES). Under this agreement, FES assumed the supply obligation for the portion of the POLR power supply requirements that are not self-supplied by Met-Ed and Penelec. FES sells this power to Met-Ed and Penelec based upon their respective shopping credits. FES has hedged most of the Met-Ed and Penelec unfulfilled POLR obligation through 2005, the period during which deferred accounting was previously allowed under the Commission's order.

Because FirstEnergy had already reserved for the deferred energy costs and FES has largely hedged the anticipated POLR energy supply requirements for Met-Ed and Penelec through 2005, we believe that the disallowance of CTC recovery of POLR costs will not have any significant adverse financial impact on FirstEnergy.

It should be noted that Met-Ed and Penelec will continue to use deferred accounting for their non-utility generation (NUG) contract costs in excess of market value. The deferral of above-market NUG costs was not an issue appealed to the Commonwealth Court.

- **Merger Savings**

The Commonwealth Court remanded the merger savings issue back to the Commission to determine the amount of merger savings and the allocation of those savings. The Company believes that the Commonwealth Court did not realize that cost savings estimated in the merger proceeding were, in fact, the same thing as merger savings. The Commission's order had addressed the sharing of estimated cost

savings through a three-year extension of the distribution rate cap at Met-Ed and Penelec.

It is possible that the Commission may choose to initiate further administrative proceedings to address the Court's remand.

### **Pensions and Other Postretirement Benefits**

In FirstEnergy's third quarter 2002 SEC Form 10-Q, we discussed anticipated pension and other postretirement employee benefit costs and funding for 2003. Those estimates have been finalized and are summarized as follows:

- The Company's assumptions in determining pension and other postretirement benefit costs and funding for 2003 are a return on plan assets of 9.0%, a discount rate of 6.75%, and a compensation increase of 3.5%. These compare to 9.5%, 7.25%, and 4.0%, respectively, as used in our estimates for the third quarter SEC Form 10-Q.
- Under ERISA minimum funding requirements, we did not make a cash contribution to the pension plan in 2002 and are not required to make one in 2003.
- In the fourth quarter of 2002, FirstEnergy recorded a non-cash, after-tax charge to equity (through other comprehensive income) of \$448 million to recognize a minimum pension liability under SFAS No. 87. This compares to our prior estimate of \$328 million that was based on the preliminary assumptions mentioned above.
- FirstEnergy's non-cash, pre-tax pension and other postretirement expense under SFAS No.87 and 106 will increase by \$170 million in 2003 as compared to 2002. This compares to our prior estimate of \$165 million. This represents an increase of \$125 million in pension expense and \$45 million in other postretirement expenses such as health care.

As we noted in previous letters, FirstEnergy uses the actual market value of plan assets to calculate annual pension costs. This is the most conservative approach because it immediately and fully reflects the impact of actual investment results in annual pension costs. Many companies use an "asset smoothing" methodology that can average the value of plan assets over periods as long as five years. Such asset smoothing results in a lower volatility of reported earnings.

### **Asset Retirement Obligations**

As a result of implementing SFAS No. 143, Asset Retirement Obligations, as of January 1, 2003, FirstEnergy has determined that the impact of this new standard will be to increase common stockholders' equity by \$181 million. This will partially offset the effect of recognizing the minimum pension liability under SFAS No. 87 described above. The cumulative effect of this

accounting change will be an increase of \$0.57 per share to the Company's reported net income in 2003. This amount is not included in our earnings guidance for 2003.

### **Assets Pending Sale**

Emdersa is an electric distribution company in Argentina formerly owned by GPU, and was acquired by FirstEnergy when the merger with GPU was completed in November 2001. Emdersa was one of the international assets identified for divestiture within one year of the merger with GPU. FirstEnergy had classified Emdersa's assets and liabilities in the Consolidated Balance Sheet as "Assets Pending Sale" and "Liabilities Related to Assets Pending Sale". In addition, earnings contribution from this business was excluded from our earnings guidance.

As of December 31, 2002, FirstEnergy neither completed the sale nor reached a definitive agreement to sell Emdersa. Therefore, these assets will no longer be classified as "Assets Pending Sale" on FirstEnergy's Consolidated Balance Sheet and Emdersa's results of operations will now be included on FirstEnergy's Consolidated Statement of Income. As a result, FirstEnergy will record in the fourth quarter a one-time, non-cash "Cumulative Effect of Accounting Change" on its Consolidated Statement of Income related to Emdersa's cumulative results of operations from November 7, 2001 through October 31, 2002. The amount of this one-time, after-tax charge was \$88.8 million, or \$0.30 per share (comprised of \$104.1 million in currency transaction losses arising principally from U.S. denominated debt, offset by \$15.3 million of operating income).

On November 1, 2002, FirstEnergy began consolidating the results of Emdersa's operations in its financial statements. In addition to the currency transaction losses of \$104.1 million, FirstEnergy will recognize a currency translation adjustment in other comprehensive income of \$91.5 million as of December 31, 2002, which will reduce FirstEnergy's common stockholders' equity. This adjustment represents the impact of translating Emdersa's financial statements from its functional currency to the U.S. dollar for FirstEnergy's financial reporting.

### **Earnings Guidance**

None of the issues discussed in this investor letter modifies our earnings per share guidance for 2003, which remains at \$3.35 to \$3.55. This guidance excludes Davis-Besse outage costs and the cumulative effect of SFAS 143.

### **Fourth Quarter Earnings Release**

FirstEnergy will release its fourth quarter 2002 financial results on Thursday, February 13, 2003. A conference call with investors will be held at 1:30 PM that afternoon. Details of the call and its Webcast will be detailed in a news release, which will be issued several days in advance of the call.

If you have any questions concerning information in this update, please call Kurt Turosky, Director of Investor Relations, at (330) 384-5500, or me at (973) 401-8519.

Very truly yours,

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