Testimony of
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Electric Reliability Involving the Closing of Plants In Greene County

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Good morning, I'm Jim Lash, President of FirstEnergy Generation. Thank you for the opportunity to testify.

FirstEnergy is the largest electricity provider in Pennsylvania, serving more than 2 million customers across the state through our regulated electric distribution companies – Penelec, Penn Power, West Penn and Met-Ed. Our 10 electric distribution companies also serve customers in Ohio, New Jersey, West Virginia, Maryland and New York.

Our diverse generating fleet has a current capacity of more than 20,000 megawatts. Today I am here to talk about changes in our Pennsylvania generation fleet, a portion of our business that sells power in the competitive wholesale and retail markets.

As you know, on July 9 we announced our decision to deactivate the Hatfield's Ferry and Mitchell power stations. Hatfield's Ferry Power Station is a coal-fired power station located in Masontown, and has a generating capacity of 1,710 megawatts. Mitchell Power Station is a coal-fired power station located in Courtney, and has a capacity of 370 MW. Together, these two plants comprise about 10 percent of FirstEnergy's total generating capacity. We intend to close both plants by October 9, 2013.

Closing plants is never an easy decision and it's not a decision we take lightly. These planned closures affect 380 of our colleagues, and have ramifications throughout our entire organization. Our decision to close Hatfield's Ferry and Mitchell was in no way a reflection on the fine work performed by our employees at these facilities.

My job is to run electric generating plants, not to close them. However, while deactivating plants is an unpleasant choice, it was unfortunately the necessary choice for both Hatfield's Ferry and Mitchell.

Our decision to close these plants needs to be understood within the context of the regional electric utility industry. Much of our generating fleet depends on revenues from the wholesale and competitive retail markets. And, as you may know, one consequence of our nation's prolonged economic slump is that the wholesale and competitive retail energy markets are depressed. Due to the abundance of natural gas – including gas from the Marcellus Shale formation here in Pennsylvania – and other market pressures, market prices for electricity are at historic lows. Costs, however, are increasing, driven primarily by state and federal regulatory mandates – usually environmental mandates. Many companies have announced plant closures, and some merchant generating companies, including most recently the Longview Power company in West Virginia, have entered bankruptcy proceedings.

We conduct economic analyses on all of our generating stations on an ongoing basis, and it is apparent that the slow economy and cost of upcoming environmental regulations have made continued operation of Hatfield's Ferry and Mitchell uneconomical. This conclusion is supported by the PJM Independent Market Monitor's market power analysis, which also determined that these units are uneconomical. Similar analyses in the past have resulted in plant closures in regulated states and unregulated states, and at union facilities and non-union facilities.

Low demand for power and low electricity prices continue to affect our business seven years into the economic recession. Although we have seen some slight economic improvements recently, residential demand for power has remained relatively flat, commercial deliveries are down approximately 6 percent, and industrial deliveries are down about 8 percent since 2007. In fact, FirstEnergy's Pennsylvania utilities collectively serve fewer customers today than they did in

2007. And as a result of low demand and a surplus of low-cost natural gas, wholesale electricity prices today are about half of what they were just a few years ago. While low electric prices are good for consumers, current low revenue streams for Hatfield's Ferry and Mitchell mean that these plants are losing money, and are projected to operate at a financial loss for the foreseeable future.

Hatfield's Ferry and Mitchell power stations failed to clear the 2016-2017 PJM base residual capacity auction, and some of the individual units at these stations have not cleared that auction for several years. The PJM capacity auction and markets were created to keep existing generation running and encourage the construction of new generation through capacity payments – payments made in exchange for making electrical capacity available.

When energy revenues are low, capacity payments should be high, and vice versa – ultimately ensuring sufficient revenues through a combination of energy and capacity payments. In recent years, however, energy prices have been at historic lows, yet the capacity auction prices have not offset those losses. The market is not achieving its purpose of retaining existing generation and encouraging construction of new generation where it is needed. I have to say here that the effects of market dysfunction are not limited to the Hatfield's Ferry and Mitchell plants. The simple fact is that if the markets do not generate sufficient revenues, more plants will close and new generation will not come online.

FirstEnergy and other industry leaders have and will continue to express concerns about the need for change to PJM's energy markets. FirstEnergy is committed to working with PJM and others to ensure that the markets perform their intended function of retaining existing generation and encouraging new generation. However, we cannot continue to operate the Hatfield's Ferry and Mitchell power stations at a loss while changes to the PJM markets are discussed.

Low capacity revenues are one piece of the financial analysis. As I noted above, costs to comply with environmental regulations are an important part of the equation. Specifically, substantial investments would be required to bring the Hatfield's Ferry and Mitchell power stations into compliance with the Obama administration's upcoming environmental regulations, including the Mercury and Air Toxics Standards (MATS) rule that is set to take effect in 2015. Together, the plants need approximately $270 million in equipment upgrades to comply with the pending MATS rule. We simply can't justify making that kind of investment at plants that are already losing money.

The new environmental equipment required at Hatfield's Ferry under the MATS rule is in addition to the scrubbers installed there in 2009, which cost $715 million and were built to comply with regulations that were in place at that time. I'd like to take this opportunity to correct the misperception that ratepayers are bearing the costs of these scrubbers. Ratepayers did not pay for the scrubbers. The scrubbers were funded through a combination of cash and state-authorized, tax-exempt bonds. Those bonds have been and will continue to be paid entirely by FirstEnergy's shareholders. In fact, FirstEnergy shareholders have been responsible for capital investments at our merchant generating facilities in Pennsylvania since deregulation in the late 1990s.

The MATS rule is only the beginning of the required capital investment at these units. Other current and pending regulations call for expenditures in coal combustion byproduct disposal, Clean Water Act Section 316(b) cooling water intake structures, wastewater effluent limit guidelines, additional air emissions controls for climate change regulations, National Ambient Air Quality Standards, new source performance standards, and any costs associated with the Cross-State Air Pollution Rule (CSAPR). Ongoing uncertainty around these environmental regulations is one of the most significant challenges we face as a company, as continually changing rules make it difficult to appropriately plan and implement investments and modifications.

The bottom line is that as a result of some of the economic factors I discussed earlier, Hatfield's Ferry and Mitchell are losing money. When coupled with the need to begin making MATS investments now and the uncertainty around other pending environmental regulations, we have determined the most prudent action is to deactivate both plants by October 9. We are confident there are no reliability issues that would require us to keep the plants in operation, and we remain in ongoing discussions with PJM to ensure continued reliability.

We remain focused on deactivating the plants in a safe, secure and environmentally responsible manner while treating our employees fairly and supporting our friends and neighbors who are impacted by these closures. We hope to reassign approximately about 25 percent of the plant employees to other parts of our organization. Employees we are not able to reassign will receive severance pay and an extension of medical benefits, as well as career transition counseling and reimbursement for career training expenses.

As I said before, closing plants is never an easy decision, but given the current economic and regulatory climate, it was the only reasonable decision.

Thank you for your time today and I'd be pleased to respond to your questions.