Pennsylvania Power Company
Annual Report to Stockholders

profile '79

298

1979

The year in profile

In contrast to the previous two years, in which earnings declined, this past year showed an increase of $6.2 million in net earnings for common stock over 1978.

Two basic reasons for this marked improvement were the positive effects of the rate increase of $23.3 million which went into effect September 1, 1978, and continuing and successful efforts to constrain expenses at every level of Company operations.

Increases in kilowatt-hour sales were also positive factors in the improved picture. Kilowatt-hour sales showed a 2.9 percent rise over 1978 figures. This, plus the full year of revenue from the already noted rate increase, produced a 25.1 percent improvement in electric sales revenues. Total operating revenues were $145.3 million.

While they did not affect 1979 earnings, decisions made by the Central Area Power Coordination (CAPCO) group in January 1980 will reduce our financing burden and have a positive effect on our financial strength over the next several years.

CAPCO terminated programs involving the future construction of four nuclear generating units and delayed the scheduled completion of two nuclear units which are already under construction in which the Company has an ownership interest.

We and the other four companies in CAPCO remain convinced that nuclear energy is a safe, economical and environmentally superior method of generating electricity. Unfortunately, the increase in regulatory and political uncertainties following the accident at Three Mile Island made it highly advisable for us to reduce the level of our heavy financial commitment to this energy source.

Justin T. Rogers, Jr. and Ray E. Semmler

These decisions were not made without risk, for they will affect the supply of electricity in the future. Reliability of electric service to customers may be particularly affected in the 1990s. A more complete discussion of CAPCO construction schedule changes appears later in the report.

In June 1979 the Company sold $20 million in first mortgage bonds to finance construction programs. Approximately $6 million principal amount of pollution control notes were issued by the Company in April corresponding to a like principal amount of pollution control bonds sold by industrial development authorities, the proceeds being used to pay part of the cost of the pollution control equipment at the New Castle Power Plant and the Bruce Mansfield Plant.

COVER. On October 21, 1879 Thomas Edison produced the world's first successful incandescent electric light. This glowing filament from a replica of that light symbolizes the industry's observance of the Centennial of Light during 1979.

Financing plans during 1980 include a private sale of $22 million of first mortgage bonds (10.9% Series) to a group of insurance companies and a private sale of $10 million of 10.5 percent preferred stock to a single insurance company. Late in the year we plan to sell to our parent company, Ohio Edison, 340,000 shares of common stock (par value $30, total $10.2 million). Approximately $2 million will be obtained through the issuance of a pollution control note in the summer of 1980. A portion of this total of $44.2 million was used March 1, 1980 to retire at maturity $3 million of first mortgage bonds (2-3/4% Series). The remainder will be used for new construction and improvement of existing facilities. Approximately $59.6 million has been budgeted for such work in 1980.

As noted earlier, our present financial health is somewhat better than that of the previous two years. But inflation continues its nagging process of erosion, rising 25 percent since the test year which was used as we sought the rate increase mentioned above. That test year was for the 12 months ended July 31, 1977. Thus we have applied to the Pennsylvania Public Utility Commission for an $18 million increase in rates. Application for the increase was filed January 16, 1980, to become effective for all retail customers on and after March 17, 1980. On February 15, 1980 the Commission suspended the increase pending further proceedings.

The Company's first mortgage bond ratings have not changed. Moody's presently gives us a Baa rating on our first mortgage bonds, while Standard & Poor's gives us an A rating.

Meeting air and water pollution control requirements has been a most challenging problem for the past several years. The problem remains with us, even though our total estimated expenditures over several years amount to $61 million or more for air and water quality and other environmental requirements. One of the most difficult problems involves sulfur dioxide emissions at our New Castle Power Plant. A continuing series of meetings with representatives of the Pennsylvania Department of Environmental Resources (DER) has sought solutions to this issue. At the present time we are awaiting that agency's response to certain proposals suggested as solutions by the Company. More detailed information concerning this important matter and other matters in litigation appear later in this report.

The Company lost a valued member of its board when Wesley S. Hodge, director since 1965, died July 4, 1979. We shall miss his counsel, his experience as a business and industrial leader and his friendship.

John R. White, chairman of the board since 1975, elected to take early retirement effective December 31, 1979. The past five years have been among the most difficult in the history of the utility industry and we are grateful for his effective leadership.

While columns of statistics and rows of figures are the heart of any annual report, our major asset is our strong team of employees whose daily dedication to providing good service often requires more than ordinary effort. We sincerely appreciate their talented contributions and continued support.

Justin T. Rogers Jr.

Chairman of the Board

President

New Castle, Pennsylvania
March 11, 1980

Highlights

Total operating revenues were $145.3 million, a 22.01% increase.

On July 16, 1979, a new system peak load of 554,000 kilowatts was recorded and on August 1 this mark was equalled.

Industrial kilowatt-hour sales reached 1.9 billion, showing an increase for the fourth consecutive year.

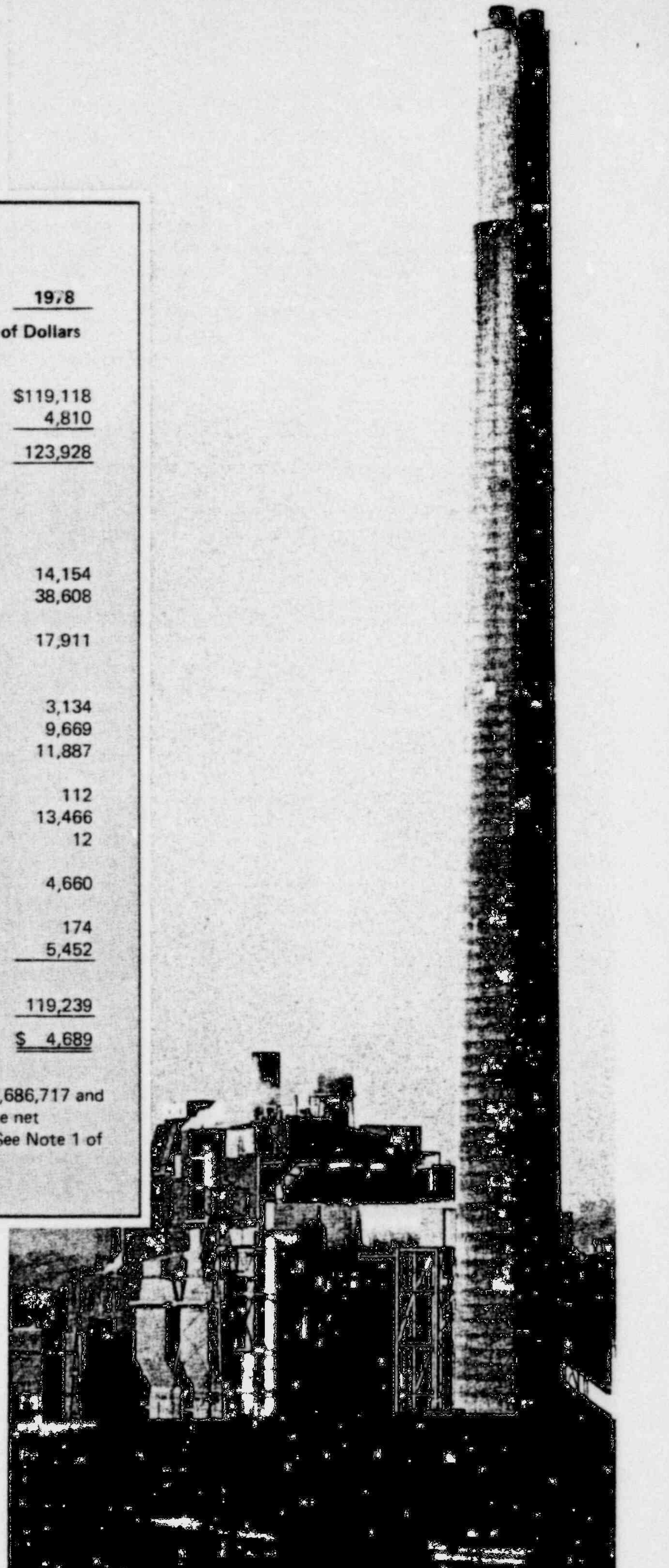
CAPCO group terminated plans to build four nuclear generating units in major construction cutback.

Average annual use per residential customer was 7,626 kilowatt-hours, a drop of 53 kilowatt-hours, first year since the early 1930s to show a decrease in average annual use.

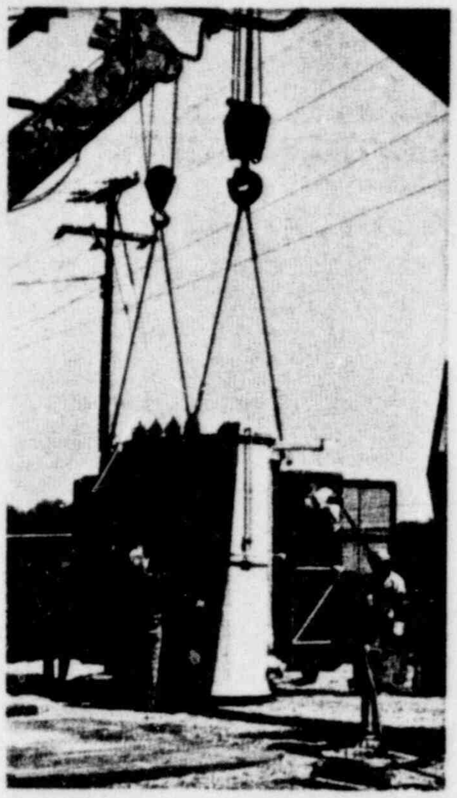
Brief Financial Summary

	1979	1978
REVENUES RECEIVED:	Thousands of Dollars	
Operating revenues—		
From sale of electricity and miscellaneous revenues	$145,340	$119,118
Other income - net	6,297	4,810
Total	151,637	123,928
REVENUES PROVIDED FOR:		
Wages to employees, including costs of pensions, group life insurance, hospitalization and other benefits	14,978	14,154
Cost of fuel (1)	45,587	38,608
Materials and supplies and other expenses	17,649	17,911
Electricity purchased, plus net interchange with other electric utility companies	7,516	3,134
Taxes - federal, state and local	17,672	9,669
Provision for depreciation	12,517	11,887
Amortization of debt discount, premium and expense - net	114	112
Interest expense - net	14,398	13,466
Capital stock issuance expense	—	12
Preferred stock dividend requirements	4,660	4,660
Preferred stock dividends declared in excess of requirements	—	174
Common stock dividends	12,278	5,452
Total	147,369	119,239
RETAINED EARNINGS	$ 4,268	$ 4,689

(1) Amounts for 1979 and 1978 include an increase of $1,686,717 and a decrease of $1,175,344, respectively, representing the net amortization of the previously deferred energy costs. See Note 1 of Notes to Financial Statements on page 28 herein.



POOR ORIGINAL



LEFT. J. A. Elser, right, Zelienople District customer services representative, and builder check plans of total electric apartment complex in Mars, PA.

RIGHT. Substation crews move transformer during construction to increase capacity of Chippewa Substation.

MONEY:

where it came from, where it went

A new system peak load of 554,000 kilowatts was established July 16 and equalled August 1.

Total kilowatt-hour sales were 2.9 percent higher than in 1978. Kilowatt-hour sales showed an increase of 93,767,284 over 1978, while total electric sales revenues increased 25.1 percent to $134.7 million.

The previous year's rate increase of $23.3 million and increased fuel prices affected all retail rate classes and raised the average residential rate to 5.64 cents a kilowatt-hour compared to 4.56 cents a kilowatt-hour in 1978.

Average use per residential customer was 7,626 kilowatt-hours compared to 7,679 kilowatt-hours in 1978. The average annual residential bill was $430.01 compared to $349.84 in 1978.

This was the first year since the depression years of the early 1930s that the average residential kilowatt-hour use per customer failed to gain over the previous year, although total residential kilowatt-hour sales did increase 1.1 percent.

It should be noted that 1979 was a year without the usual extremes of weather, resulting in less use of heating and air conditioning in many homes. This was compounded by lower general use because of higher energy costs. It was also a year which saw a slowing economic pace in its latter months.

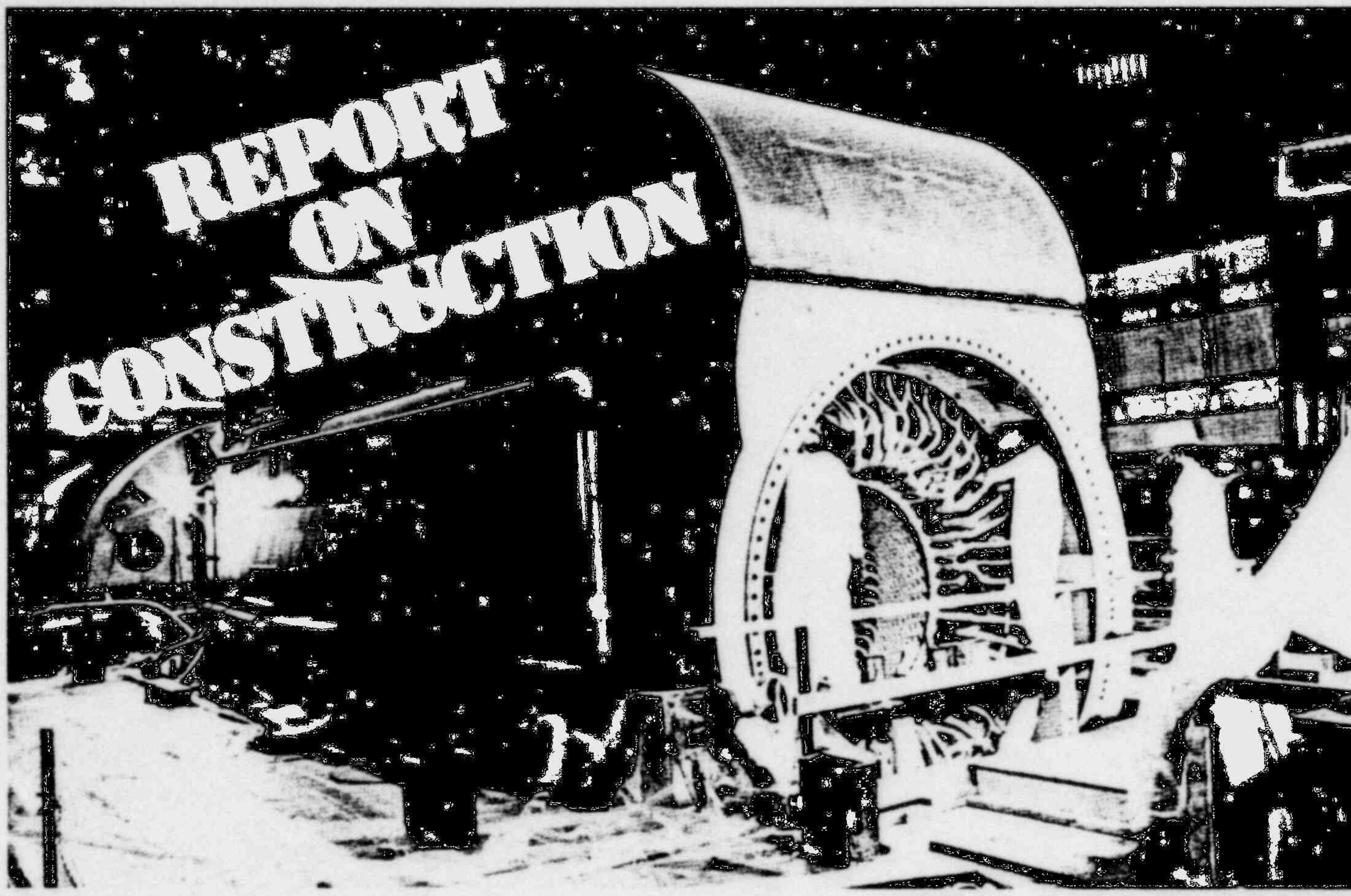
The limited growth in the residential area was offset to some degree by the record of industrial and commercial use. Industrial kilowatt-hour sales have shown a solid growth trend for the past three years. Industrial sales for 1979 rose by 3.4 percent to a level second only to the high established in 1973. Commercial kilowatt-hour sales rose 3.7 percent.

Total operating expenses were $85.7 million, compared to $73.8 million in 1978. These expenses per kilowatt-hour sold were 2.56 cents compared to 2.27 cents in 1978.

Part of the increase in operation and maintenance costs was due to extensive turbine repairs to Unit No. 5 at the New Castle Power Plant and the use of more expensive low-sulfur coal since June at the plant. Unit No. 5 was out of service from February 9 to June 7. In addition, the Beaver Valley nuclear station was out of service from March 13 to August 20 for the Nuclear Regulatory Commission (NRC) design investigation and required modifications. Resuming production in August, it again was taken out of service December 1 for refueling and further modifications. It is not expected to return to production until July 1980.

Loss of production from these two stations required the operation of less efficient units and also caused purchased and interchanged power costs to increase $4.4 million.

Total operating taxes increased to $17.7 million from $9.7 million in 1978. Interest charges rose, amounting to $18.8 million, due principally to the sale of first mortgage bonds June 28, 1979.



Workmen at the generator of Unit No. 3 at the Bruce Mansfield Plant. Unit No. 3 is scheduled for commercial operation in October 1980.

Most of the Company's construction funds are allocated for generating facilities in conjunction with the construction program of the CAPCO group.

This five-company group, in addition to the Company and Ohio Edison, consists of The Cleveland Electric Illuminating Company, Duquesne Light Company and The Toledo Edison Company.

Since the CAPCO program began, three coal-fired units and one nuclear unit in which the Company has ownership interests have been completed. A fourth coal-fired unit, Bruce Mansfield Unit No. 3, is scheduled to go into commercial operation in October 1980. The Company is the builder and operator of the Bruce Mansfield Plant for the CAPCO group. The plant is located at Shippingport, PA.

On three occasions, in 1974, 1977 and 1978, the CAPCO companies revised construction schedules for generating units. Forecasts indicated a slowing of customer electricity needs, and the resulting construction slowdown eased to some degree the need for the huge amounts of construction capital.

In mid-January 1980 the CAPCO group announced major cutbacks in its construction program, terminating four nuclear units and extending construction periods for two other nuclear units in which the Company has ownership interests.

The four units terminated by this action were Units Nos. 2 and 3 at the Davis-Besse Nuclear Power Station near Port Clinton, Ohio and Units Nos. 1 and 2 at the Erie Nuclear Plant north of Berlin Heights, Ohio. At the time of termination all of these units were in the design stage.

Total estimated cost to build the four terminated units was $7.3 billion, with the Company's share being $455 million.

Perry Unit No. 1 has been rescheduled from May 1983 to May 1984. Perry Unit No. 2 has been rescheduled from May 1985 to May 1988.

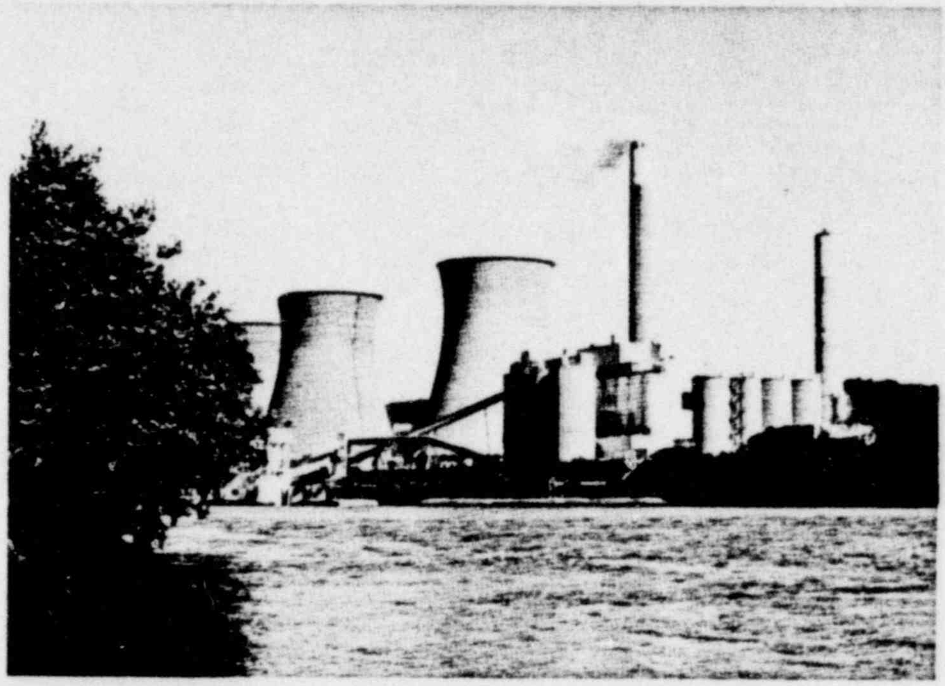
Below are the various CAPCO units and the Company's present share of ownership.

Coal-fired

Bruce Mansfield No. 1....	4.2%
Bruce Mansfield No. 2....	6.8%
Bruce Mansfield No. 3....	6.28%
W. H. Sammis No. 7	20.8%

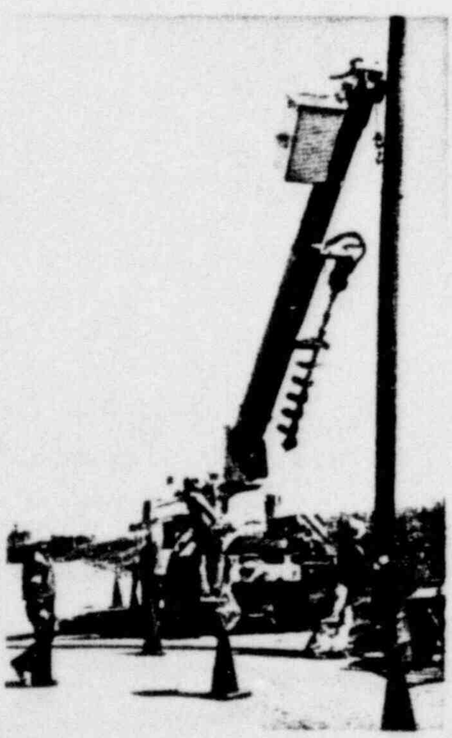
Nuclear

Beaver Valley No. 1.....	17.5%
Perry No. 1	6.28%
Perry No. 2	6.28%



Figures published by the Pennsylvania Electric Association (PEA) in mid-1979 show that demand growth for the state's electric utilities in the eight years between 1966 and 1973 averaged 6.9 percent. In the period following the Arab oil embargo 1974 to 1978, demand declined in two of the five years and annual growth averaged only 1.6 percent in the state. The revised projected rate of growth in customer demand for electricity for the CAPCO group of companies, who serve about 2.5 million customers in northern and central Ohio and western Pennsylvania, is in the range of 2 to 4 percent each year.

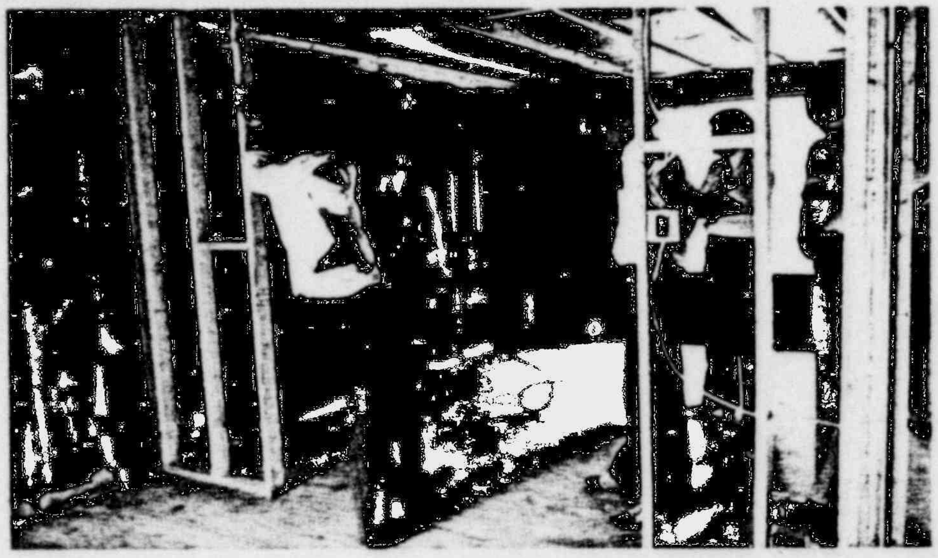
Expenditures of $62.0 million were authorized for 1979 by the board of directors. A total of $57.6 million was expended for construction, $45.7 million of that amount being utilized for power plant construction. Most of the remainder was utilized in substation construction and expansion and for transmission line construction.



LEFT. New Castle line crew, under direction of Foreman W. L. Doran, replaces a pole along a country road.

TOP. The coal-fired Bruce Mansfield Plant along the Ohio River at Shippingport, PA. Its three units will have a net dependable capability of 2,475 megawatts.

Serving Customers



...residential

...commercial

...industrial

ABOVE LEFT. Residential customer services representatives with builders in New Castle area check insulation techniques.

ABOVE RIGHT. J. F. Haas, left, energy application engineer, and owners and operators of a New Castle plastics manufacturer with a few of their many products.

CENTER. Worker pours molten metal from electric furnace. Ever growing use of electric furnaces in area industries is contributing heavily to industrial scles.

POOR ORIGINAL

Four principal objectives guided the Company's marketing activities during the year.

These were to:

* Improve the economic utilization of Company facilities;
* Assist and encourage customers to use electricity wisely;
* Maintain favorable customer attitudes toward the Company and the value of electric service;
* Assist area communities to maintain a healthy economy.

Again this year, as in 1978, the Company's efforts to shift industrial loads to off-peak periods showed definite progress. Six thousand seven hundred fifty kilowatts were shifted to off-peak by industrial customers. Annual system load factor increased from 71.0 percent to 71.6 percent.

Load meters and off-peak water heating rates for residential customers have for years been a useful method of controlling system loads. Peak load and power factor-sensitive billing is employed for the majority of industrial and commercial customers, enabling these customers to realize economies in their operations and simultaneously improve our system load factor.

Electric heat pump installations have continued their steady rise, a pattern of growth continued in our area for several years.

Growing customer acceptance of the heat pump is most evident in the residential area. The past year was excellent for new home construction: 547 heat pumps were installed compared to 322 in 1978. A total of 590 all-electric residential installations were added to our lines, bringing the total to 3,383, an increase of more than 21 percent over 1978.

Workshops and seminars held during the year, and close-working relationships with architects and builders, emphasizing the importance and economics of energy management, were key elements which encouraged this growth pattern. School programs and public meetings, conducted by the Company's home economics representatives, continued to disseminate useful energy information. During the year 1,441 school, home and public programs were conducted.

In addition to the usual on-the-job assistance given by Company customer service representatives to builders, a new element was introduced during the year, a videotape camera. Recording proper equipment installation and insulation techniques has upgraded the quality of workmanship and materials and has been helpful to builders in meeting required energy conservation standards.

A majority of home builders in our area are complying with the standards set in the "Easy on Energy Homes" program and all builders are kept informed as requirements or changes are made in construction or insulation standards. This program has been in effect for nearly three years.

While total-electric homes have been growing in number, the average energy use in such homes has shown a gradual decline. This, in part, is due to improving construction and insulation techniques and also because of the growth of heat pump installations, which use less energy than resistance heating.

During 1979, 12 of the Company's 18 largest industrial customers showed increases in kilowatt-hour use. New industrial load connected during the year totaled 20,444 kilowatts compared to 18,873 kilowatts in 1978.

The past year was excellent in respect to expansion programs by area industries, with 11 expending more than $36.5 million, providing employment for 227 workers. The Company's area development representatives, working with community, county and state development groups, attracted 16 new firms to our service area, representing a capital investment of more than $6.7 million and 380 new jobs.

POOR ORIGINAL

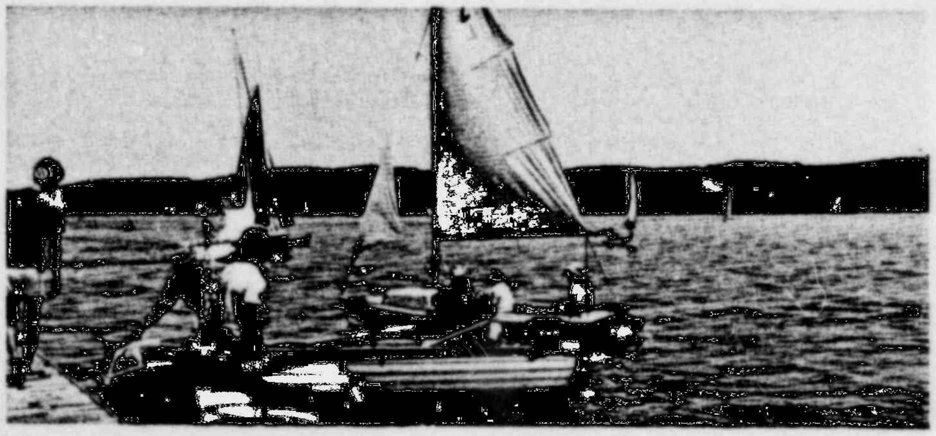
Awards were presented 14 builders who constructed five or more "Easy on Energy Homes" during the year. J. A. Elser, left, and C. W. Beighey, right, customer services representatives in the Zelienople District, with builders.

TOP TO BOTTOM. *High pressure sodium vapor lights were installed on East Washington Street in New Castle's renovated downtown business district.*

Life-size Reddy Kilowatt captured attention of child at Lawrence County Farm Show.

J. A. Elser at solar home in Zelienople District which has heat pump for basic heating requirements.

Moraine State Park, about 12 miles east of New Castle, continues to grow as a major recreation area.



Problems persist

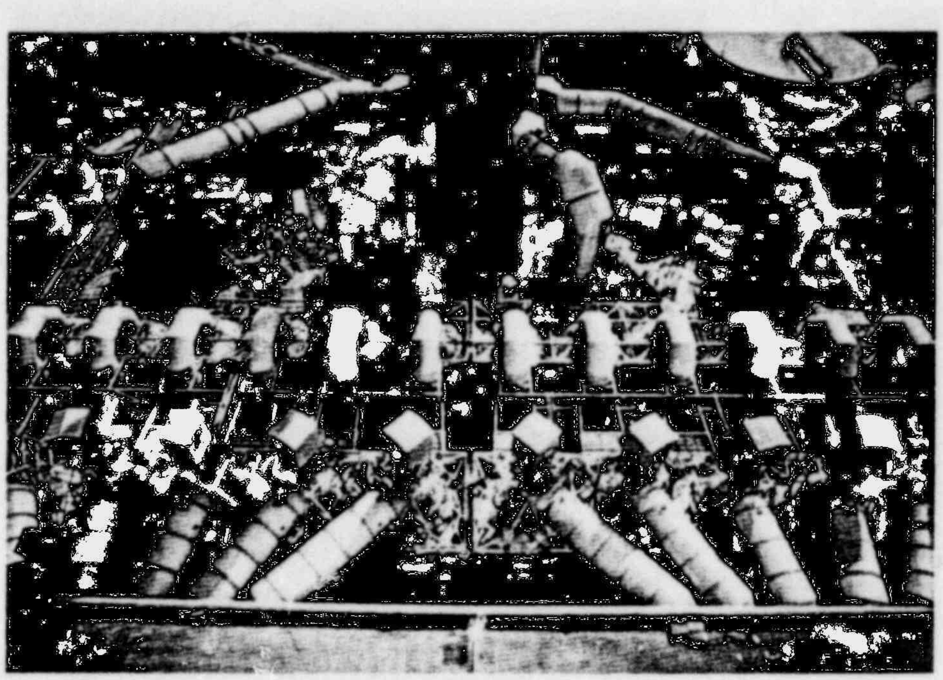
legal/environmental

Through its participation in the CAPCO arrangement and because of construction of facilities in both Ohio and Pennsylvania, the Company is subject to environmental regulations in those states in addition to federal regulations.

Several legal proceedings are underway and various negotiations are continuing with environmental authorities seeking reasonable arrangements that will have the least economic impact on the Company and on its customers' electric bills.

The United States Justice Department, at the request of the Federal Environmental Protection Agency (EPA), filed suit against the Company on May 16, 1979, alleging the Company's New Castle Power Plant has been in continual violation of the Pennsylvania Department of Environmental Resources (DER) rules and regulations for sulfur dioxide (SO_2) emissions since prior to August 7, 1977. The suit requests that the Court impose civil penalties of $25,000 per day for the alleged violations.

On December 18, 1978 the Company was served with an amended complaint joining it in a legal proceeding begun August 2, 1978, by the federal government against Duquesne Light Company and Ohio Edison Company as co-owners of W. H. Sammis Unit No. 7.



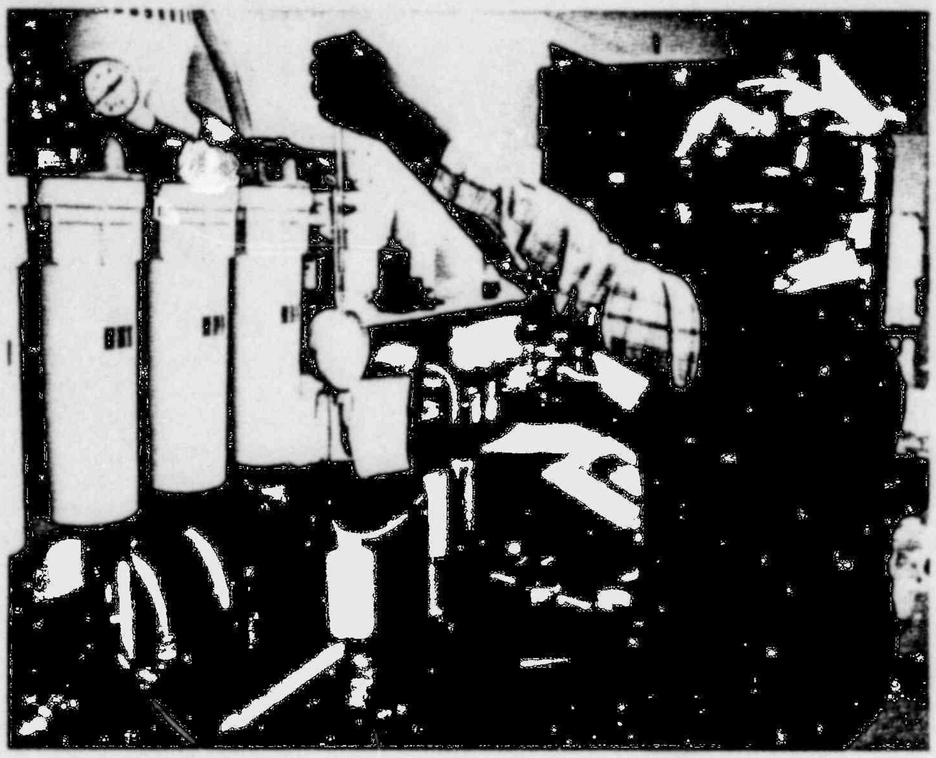
This pattern of vessels and maze of pipes is the air quality control system for Units Nos. 1 and 2 at the Bruce Mansfield Plant.

The proceeding brought in the United States District Court for the Southern District of Ohio, Eastern Division, asks the District Court to assess "appropriate" but unspecified civil penalties for alleged violations of particulate emission regulations promulgated under the Clean Air Act.

The Company has submitted proposed regulation changes for the New Castle Power Plant and compliance schedules for the W. H. Sammis Unit No. 7. If such proposals are not accepted by the environmental agencies, substantial civil penalties may result. If it is necessary to install additional equipment to satisfy any court order, the capital cost of such equipment could be approximately $85 million at the New Castle Power Plant and $26 million for the Company's share of the W. H. Sammis Unit No. 7.

The Clean Air Act Amendments of 1977 include, among other things, provisions requiring the imposition of substantial noncompliance penalties for failure to comply with applicable emission limits after August 7, 1979, with certain exceptions. Even if the proposed changes and schedules submitted for the New Castle Power Plant and W. H. Sammis Unit No. 7 are accepted by the environmental agencies, substantial noncompliance penalties may result. In addition, the Company could be forced to shut down those plants that do not comply. The effect of any such shutdown on the costs to and operations of the Company is not presently determinable, but it

POOR ORIGINAL



L. L. Hill, laboratory analyst, conducting one of a variety of tests in the laboratory at the Bruce Mansfield Plant.

could require purchases of power at prices significantly greater than the Company's cost of generation.

The Company has pending a request for a variance from the thermal requirements of the water discharge at its New Castle Power Plant with the Pennsylvania DER and a request for a similar variance at the W. H. Sammis Plant is pending with the Ohio EPA. If the variances are not granted, the Company may be required to install off-stream cooling at one or both of the plants.

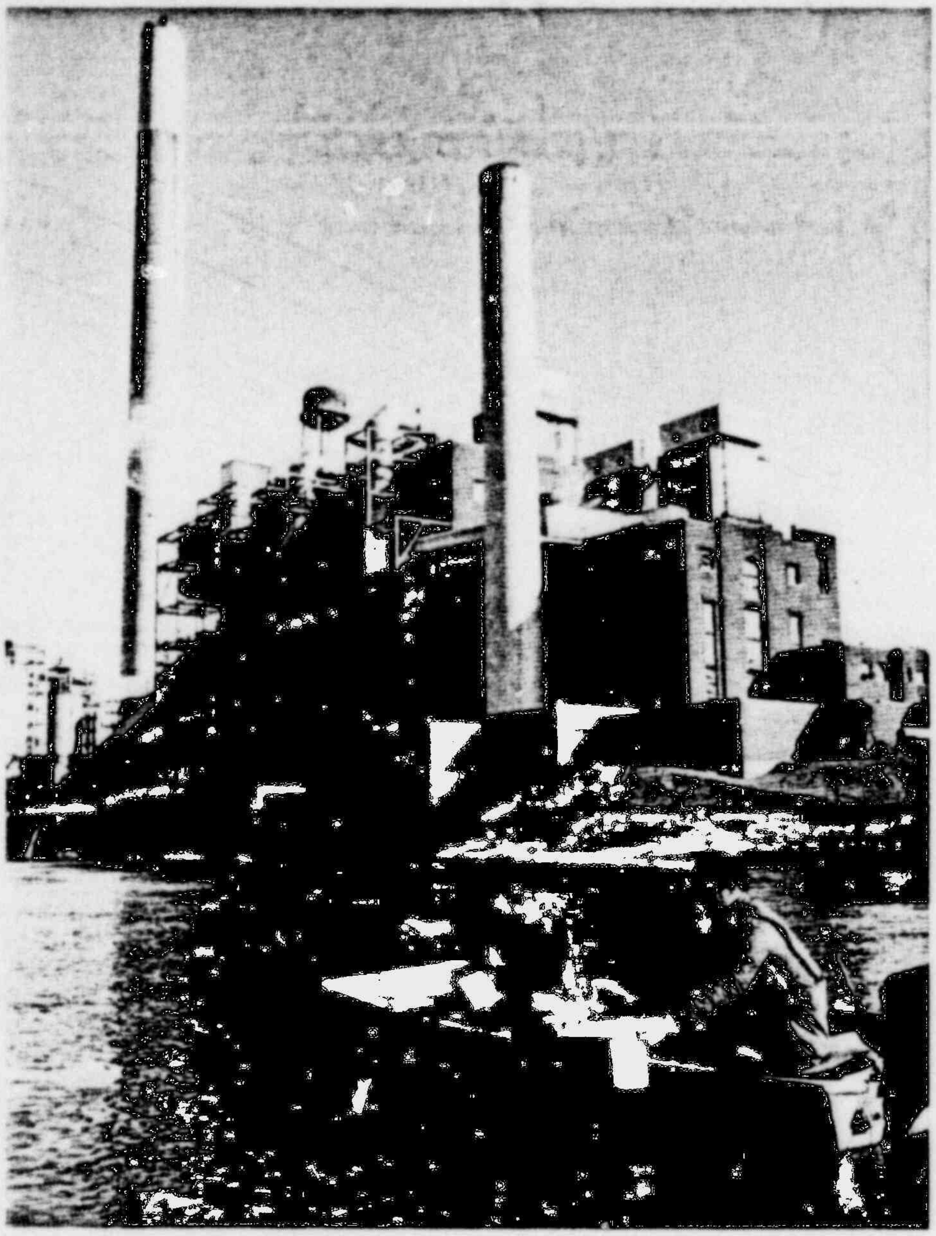
The final determination of many of these environmental matters and the financial effects on the Company is not known at this time but the effect could be substantial.

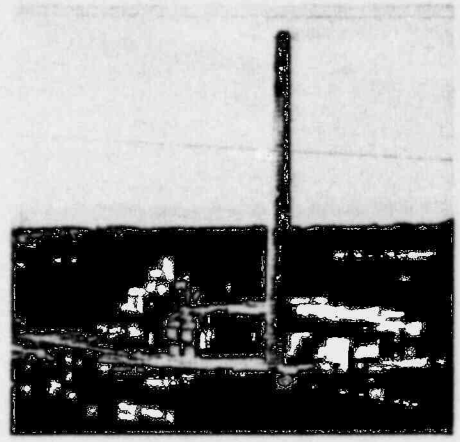
In July 1977, actions were filed against the CAPCO companies by the Borough of Shippingport, where the Bruce Mansfield Plant and the Beaver Valley Power Station are located. These actions seek to enjoin operation of these two plants. In addition, individual plaintiffs have filed actions seeking monetary relief in an unspecified amount for damages claimed to be a result of alleged operational malfunctions of the flue gas desulfurization system at the Bruce Mansfield Plant and the threat of radioactive emissions from the Beaver Valley Power Station.

A complaint, dated April 10, 1979, was filed against the CAPCO companies in the United States District Court for the Western District of Oklahoma by Kerr-McGee Corporation. The complaint concerns an alleged breach of a 1973 uranium supply contract provision relating to price adjustment and other provisions of the original contract between the two parties. The suit seeks to terminate the contract, pursuant to which Kerr-McGee Corporation is to deliver approximately 12 million pounds of uranium through 1985, and seeks damages in an unspecified amount. On June 28, 1979 the CAPCO companies filed an action for a declaratory judgment and exemplary damages against Kerr-McGee Corporation and Kerr-McGee Nuclear Corporation in the United States District Court for the Northern District of Ohio. The complaint requests the Court to declare the rights and legal relations of the parties as to disputed portions of the 1973 contract and to grant to the plaintiffs costs and exemplary damages due to defendants' unjustifiable actions in attempting to extract price increases from the plaintiffs. On September 21, 1979 the District Court in Ohio transferred this action to the Federal District Court in Oklahoma.

Two of the Company's municipal resale customers, the Boroughs of Ellwood City and Grove City, filed a complaint October 3, 1977 against the Company, alleging that the Company violated the antitrust laws in respect to access to alternative sources of power and nuclear generating facilities owned by the CAPCO companies, the "wheeling" of power to municipal systems, rate schedules and other acts concerning terms and conditions of service. The plaintiffs claimed treble damages totaling $21 million. On June 6, 1978 the Company filed a motion to dismiss or in the alternative to stay the action. The Court on January 4, 1979 granted the Company's motion in part by dismissing most of the claims, staying one claim, and allowing one claim to continue.

The PUC instituted an investigation into an outage of Beaver Valley Unit No. 1 during the period March to August 1979. The outage had been ordered by the NRC.





LEFT. Testing the water quality of the Beaver River at the New Castle Power Plant was done by a Pittsburgh firm; results will be made available to environmental and regulatory agencies.

ABOVE. The New Castle Power Plant at West Pittsburg, PA with its banks of electrostatic precipitators and 750-foot high chimney.

This pending investigation includes consideration of whether Beaver Valley Unit No. 1 should be eliminated from, or adjustments should be made in, the Company's rate base as a result of this or any outage of the unit and whether expenditures by the Company for purchased power resulting from any such outage should be disallowed for purposes of the Company's energy clause.

In a separate investigation, the PUC is considering whether additional construction costs resulting from deferral of construction projects should be excluded from rate base in subsequent rate proceedings.

Full discussions of legal/environmental issues appear in the Notes to Financial Statements in this report.

Communications

a two-way street goes on...

and on...

Seldom has any subject captured and held public attention over such a long period as that of energy and its problems.

With all of our expertise in producing and delivering electric energy, the need to explain the industry to our customers has grown proportionately with the attention energy's problems have received.

In our desire to reach as many citizens as possible with useful energy information, its costs, its problems and its benefits, the Company has for years utilized newspaper and radio advertising, regular news stories, displays and information booklets and motion picture films.

The Company's monthly news magazine for employees is nearing its 50th consecutive year of publication; a quarterly magazine known as "Profile" is now in its seventh year and continues to gain public acceptance as a publication offering a variety of credible energy information. This magazine is sent to opinion leaders in communities throughout our service area as well as to employees.

In the past 18 months, two new groups have emerged which are enhancing public understanding of the complex issues of our industry.

These two groups are a Speakers Bureau and a Consumer Information Group. The Speakers Bureau, consisting of 11 employees representing several departments in the Company, this past year presented programs on an average of once every 11 days, speaking to total audiences of 1,449. Since 1979 was designated the Centennial of Light year by the industry, marking the anniversary of Edison's invention of the incandescent light, particular attention was given this topic by the Speakers Bureau.

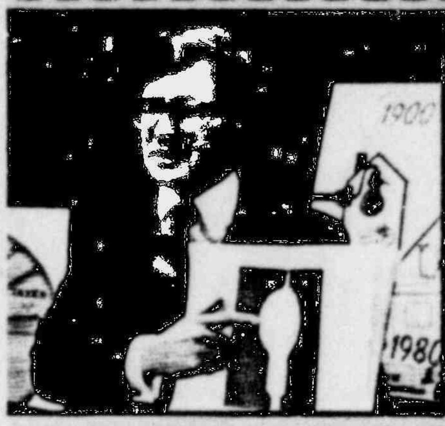
The Consumer Information Group has been meeting regularly with Company representatives since its formation nearly two years ago. Its 9 citizens represent church, civic, educational and union and senior citizen groups. Listening to the concerns of this group and simultaneously providing the group with insight into Company operations and problems is useful to both parties and serves to sensitize the Company to consumer concerns.

Power plant tours continue to be another useful communication tool, particularly at a modern coal-fired plant such as the Bruce Mansfield Plant, with its impressive array of environmental equipment. Requests for tours at this installation have been at a high level since they began several years ago. About 2,300 visitors, ranging from

ACROSS TOP OF PAGE. President Ray E. Semmler during an employee information meeting;

Gary Brown exhibiting Centennial of Light symbol during a Speaker's Bureau presentation;

One of several groups participating in Nuclear Energy Education Day (NEED) last October.



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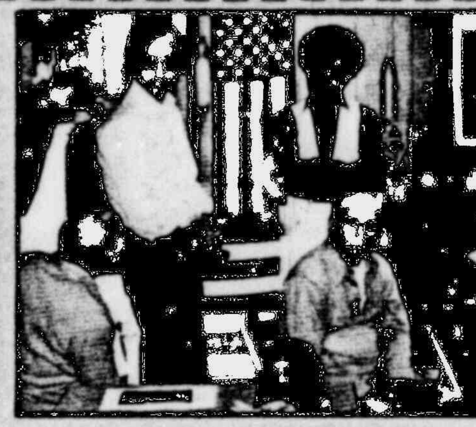


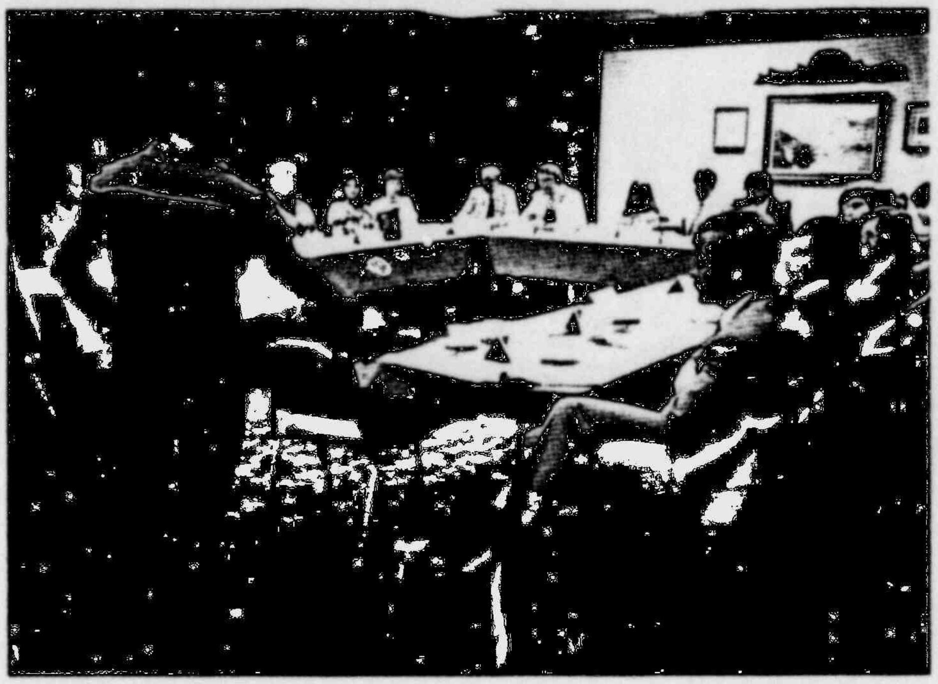
elementary school students to state legislators and engineers from foreign countries, toured the plant this past year.

When Nuclear Energy Education Day was observed nationally in mid-October, the Speakers Bureau sponsored a series of informal information sessions throughout the service area. Nuclear specialists from a major manufacturer lent their expertise to many of these sessions, which were attended by interested citizens. The event was thoroughly covered by television, radio and newspaper. Several such sessions were also held for employees.

For the second consecutive year a random, direct-mail opinion poll was taken of 500 of our residential customers. Simple in design, quickly and easily answered, the questionnaire sought customer opinions about their electric service and quality of service, nuclear energy, possible energy shortages and value of products related to price. The results indicated that 51 percent feel that nuclear energy should be used to generate electricity. With respect to price, 64 percent rated electricity in the excellent or good category and 94 percent rated their electric service excellent or good. Admittedly, a poll taken in this manner does not have the scientific approach of the professional pollsters, but we feel it does give a useful cross-section of public opinion.

In a continuing effort to expand employee understanding of Company operations and current events, Company President Ray E. Semmler for many years has conducted semi-annual special employee information meetings. Meetings have been held at locations throughout the Company area and virtually every employee has attended, with the opportunity to get answers to any and all questions about the Company.

Requests continue for tours of the Bruce Mansfield Plant. This group is in the control room at the plant.



An outside firm conducted intensive sessions during a three-day Customer Contact Workshop for employees whose work involves consumer problems.

Lessons in leadership and safety

Employment rolls continue to grow steadily, due principally to the manpower needs at the Bruce Mansfield Plant where Unit No. 3 is expected to go into operation in October 1980.

Hiring of new employees, however, has been carefully monitored in an effort to control costs.

At the close of the year the Company had 1,500 employees, compared to 1,335 at the end of 1978.

These increases plus the granting of wage and salary increases brought total wages and salaries and the cost of fringe benefits to $21.8 million, compared to $20.3 million in 1978. The cost of fringe benefits reached $492 per employee per month.

Employees represented by the bargaining unit are presently in the second year of a two-year contract. The contract with Local 140 of the Utility Workers Union of America (AFL-CIO) provided for wage increases of six percent on September 1, 1979 and an additional two percent on March 1, 1980.

Members of the International Brotherhood of Electrical Workers (AFL-CIO) received a similar six percent increase August 15, 1979 and an additional two percent on February 15, 1980.

All employees received a one percent wage increase on December 21, 1979, retroactive to October 1, 1979, in accordance with the guidelines of the President's Council on Wage and Price Stability.

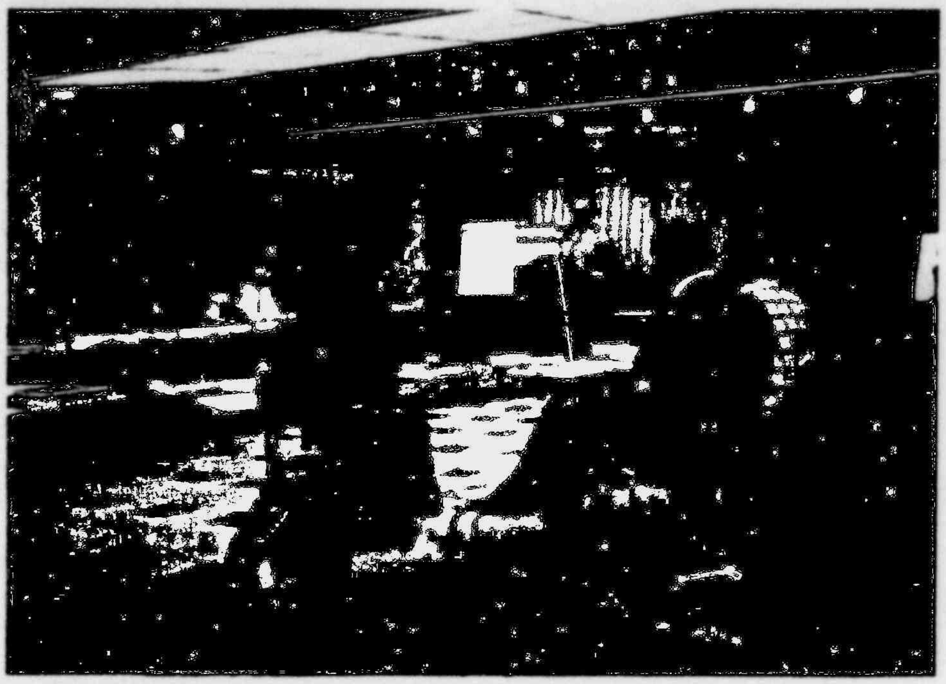
During 1979 the Company was selected, because of its small size, by the PUC to be the first electric utility to be audited by an outside consulting firm for management effectiveness. Their findings showed the Company's management techniques to be efficient, and the report was favorable to the Company.

The Company's management structure was also subjected to intensive study by outside consultants during the year and certain changes were recommended which we feel will further improve management efficiencies.

Educational programs for specific groups of employees were held during the year. Supervisory employees attended Management by Objectives sessions, while customer contact employees attended a Customer Contact Workshop which was conducted by an independent firm.

One of the most important, and perhaps most difficult, of all aspects of a company's operations lies in the area of employee safety.

Although the Company had its first lost-time accident in several years because of an electrical contact, excellent safety records have continued. The Company's



Company supervisors attended classes to study the elements of effective management.

Mercer County Substation Department has worked more than 26 years without a lost-time accident. Employees in the Zelienople District achieved 1,600 days and New Castle office employees 2,400 days without lost-time accidents. In December the New Castle Power Plant's Operating Department reached 800 days without a lost-time accident.

A single noncontributory trusteed pension plan covers all employees. At the end of the year 233 former employees and provisional payees or surviving spouses of deceased employees were receiving retirement incomes through the plan. Fourteen employees retired during the year.

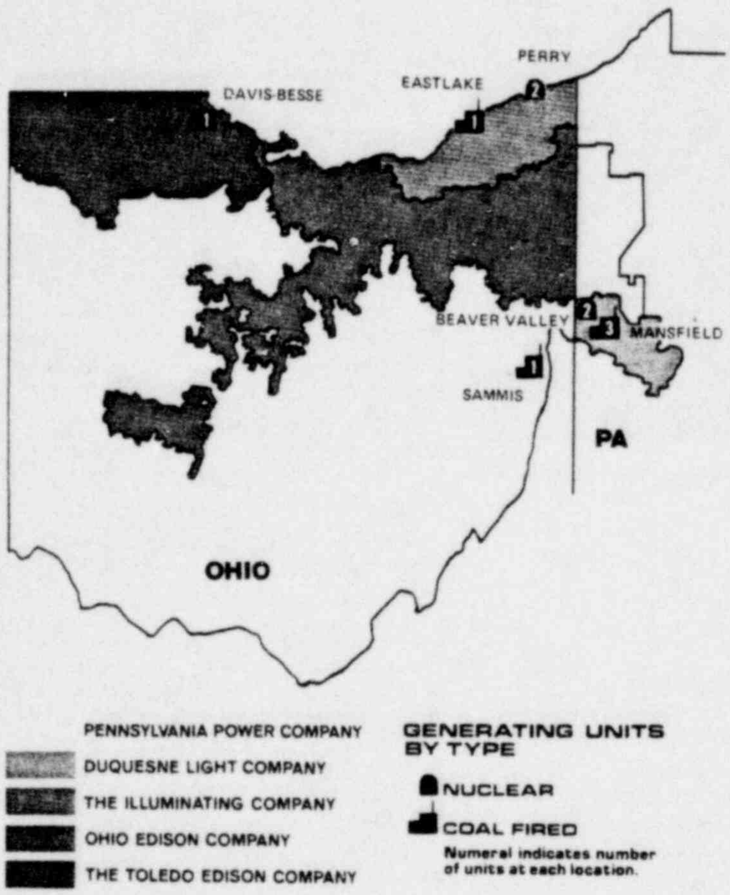
During the past year the Board of Directors had several changes in personnel. In May, Victor A. Owoc and Justin T. Rogers, Jr. were elected to the board. Mr. Owoc is executive vice president and a director of Ohio Edison; Mr. Rogers, now president of Ohio Edison, at that time was executive vice president and a director of Ohio Edison. When John R. White retired from his duties as chairman of the board on December 31, 1979, Mr. Rogers succeeded him as chairman.

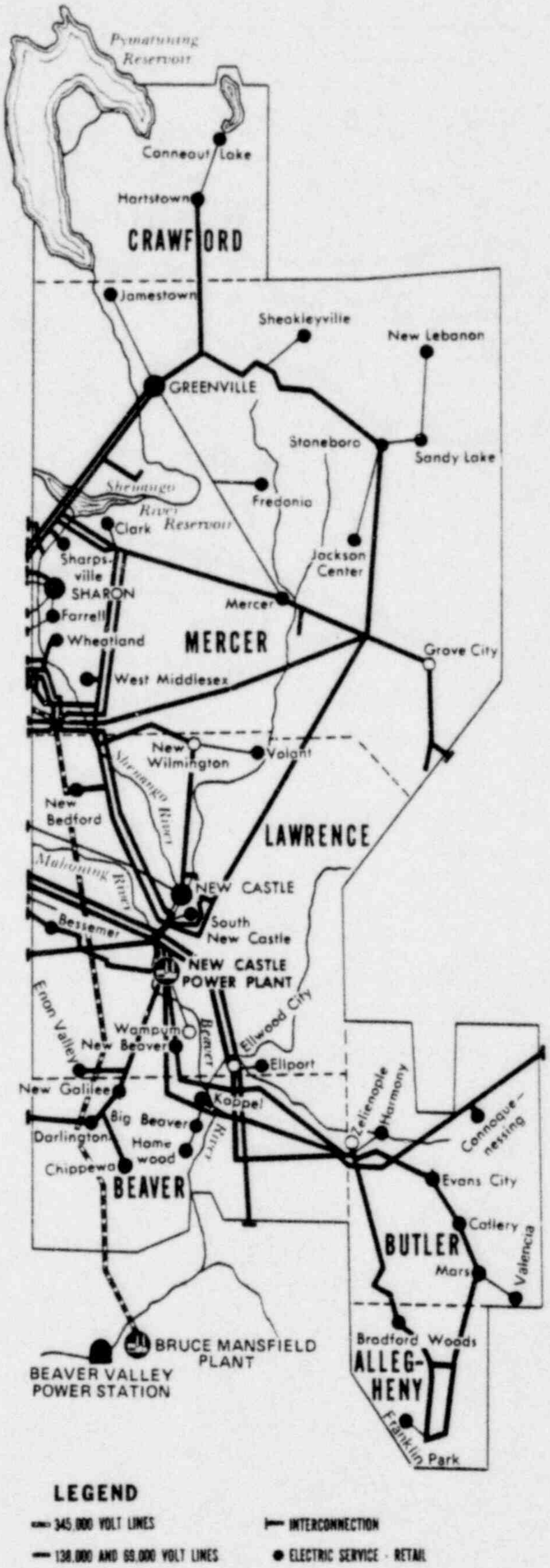
LEFT. D. E. Hackett, director, accident prevention, left, received a Certificate of Appreciation from the Pennsylvania Electric Association for serving as chairman of the PEA Accident Prevention Committee from 1977 to 1979. Ray E. Semmler, Company President and a past president of the PEA, made the presentation.

All of the Company's common stock is owned by the Ohio Edison Company, parent of Pennsylvania Power Company. At year end, the Company had outstanding nine series of cumulative preferred stock held by 3,483 shareholders. There were a total of 599,049 preferred shares outstanding. The preferred stock is listed on the Philadelphia Stock Exchange, Inc.

BELOW. L. D. Westerman, left, a member of the Zelienople District's meter department and veteran of 33 accident-free years with the Company, challenged R. W. Mann, center, a new employee in the district's line department, to match Westerman's perfect safety record. Challenge was issued during observation by all Zelienople employees as they marked 1,600 days without a lost-time accident. President Ray E. Semmler joined hands with Westerman and Mann to seal the bargain.

Service Area and CAPCO Power Pool





The CAPCO Power Pool

Five electric utility companies in Western Pennsylvania and Northern Ohio have joined together for the development of power generation and transmission facilities. Members include Pennsylvania Power Company, Duquesne Light Company, The Cleveland Electric Illuminating Company, Ohio Edison Company and The Toledo Edison Company.

Pennsylvania Power Company

Operating Statistics

	1979	1978	1977	1976	1975	1974
SALES IN KILOWATT-HOURS (MILLIONS)						
Residential*	823.3	814.7	788.3	750.5	717.9	699.6
Commercial	512.6	494.5	487.8	467.6	442.4	414.5
Industrial	1,878.5	1,816.9	1,724.5	1,704.5	1,541.0	1,832.2
All Other	130.4	125.0	123.4	112.0	104.8	105.3
Total	3,344.8	3,251.1	3,124.0	3,034.6	2,806.1	3,051.6
REVENUES FROM SALES (THOUSANDS)						
Residential*	$46,425	$37,113	$31,763	$30,643	$29,967	$24,357
Commercial	25,588	20,320	17,659	17,202	17,000	13,513
Industrial	58,128	45,201	37,085	37,786	36,547	30,844
All Other	4,540	4,994	3,555	2,955	2,465	2,500
Total	$134,681	$107,628	$90,062	$88,586	$85,979	$71,214
CUSTOMERS SERVED AT END OF YEAR						
Residential*	109,032	107,126	105,197	103,725	101,924	100,545
Commercial	12,919	12,647	12,317	12,090	11,800	11,629
Industrial	135	133	133	135	133	133
All Other	114	113	111	113	114	115
Total	122,200	120,019	117,758	116,063	113,971	112,422
RESIDENTIAL* CUSTOMER AVERAGES						
Average Kwh Used per Res.* Customer	7,626	7,679	7,548	7,301	7,099	7,018
Average Price Per Kwh— Res.* (cents)	5.64	4.56	4.03	4.08	4.17	3.48
KILOWATT-HOURS GENERATED (millions)	3,194.8	3,320.1	3,550.6	2,779.3	2,375.0	2,620.5
KILOWATT-HOURS PURCHASED AND INTERCHANGED (millions)	281.7	116.7	(205.8)	474.6	640.8	607.3
PEAK LOAD (kilowatts)	554,000	552,000	551,000	526,000	495,162	498,199

* Includes farm customers

Pennsylvania Power Company

Financial Statistics

	1979	1978	1977	1976	1975	1974
			Thousands of Dollars			
Operating Revenues	$145,340	$119,118	$100,843	$89,583	$87,212	$72,510
Operating and Maintenance Expenses	85,730	73,807	61,068	59,400	56,846	45,0[illegible]6
Depreciation	12,517	11,887	10,654	7,342	5,984	5,856
Taxes: Federal and State Income						
Currently Payable	2,241	(142)	(979)	(1,077)	5,713	2,472
Deferred (Net)	2,501	3,353	3,456	535	(126)	2,704
Investment Tax Credits (Net)	2,634	(1,458)	(554)	1,423	701	238
General	10,296	7,916	6,717	6,238	5,817	4,877
Operating Income	29,421	23,755	20,481	15,722	12,277	11,347
Other Income (Net)	6,297	4,810	5,352	13,101	12,049	8,613
Net Interest	14,512	13,578	10,322	12,304	8,941	7,484
Income Before Cumulative Effect of a Change in Accounting Method	21,206	14,987	15,511	16,519	15,385	12,476
Cumulative Effect to December 31, 1973 of Recording Metered but Unbilled Revenues (Net of related income taxes of $311,000)	–	–	–	–	–	279
Net Income	21,206	14,987	15,511	16,519	15,385	12,755
Preferred Stock Dividend Requirements	4,660	4,660	3,873	3,626	3,035	2,120
Net Income for Common Stock	$ 16,546	$ 10,327	$11,638	$12,893	$12,350	$10,635
Common Stock Dividends	$ 12,278	$ 5,452	$ 7,220	$ 8,470	$10,008	$ 3,852
Utility Plant	$546,744	$506,374	$454,522	$409,062	$350,123	$307,306
Depreciation Reserve	101,585	90,742	81,542	72,058	65,680	60,702
	$445,159	$415,632	$372,980	$337,004	$284,443	$246,604
CAPITALIZATION						
Long-Term Debt	$225,156	$205,683	$180,385	$167,813	$135,075	$117,349
Non-redeemable Preferred Stock	41,947	41,947	41,947	41,947	33,947	33,947
Redeemable Preferred Stock	17,600	18,000	18,000	8,000	8,000	–
Common Stock and Retained Earnings	154,396	150,128	140,939	118,554	106,118	98,341
Total	$439,099	$415,758	$381,271	$336,314	$283,140	$249,637
CAPITALIZATION RATIOS						
Long-Term Debt	51.3%	49.5%	47.3%	49.9%	47.7%	47.0%
Non-redeemable Preferred Stock	9.5	10.1	11.0	12.5	12.0	13.6
Redeemable Preferred Stock	4.0	4.3	4.7	2.4	2.8	–
Common Stock and Retained Earnings	35.2	36.1	37.0	35.2	37.5	39.4

Management Discussion and Analysis

Operating Revenues—

Total operating revenues increased $18,275,000 and $26,222,000 during the years 1978 and 1979, respectively. The 1978 increase was due to an increase in energy cost revenues of 28.5% and an increase in kilowatt-hour sales of 4.1%. In addition, the increase in retail base rates of 12.6% resulted from the annual increase of 40% in base rates granted by the Pennsylvania Public Utility Commission, effective September 1, 1978. Municipal resale revenues increased 56.4% as a result of implementing in September 1977 a proposed rate increase, subject to refund, pending a final decision by the Federal Energy Regulatory Commission. Surcharge revenues related to the collection of certain Pennsylvania taxes imposed on utilities, increased due to increased kilowatt-hour sales and the increase in retail base rates. The 1979 increase of 22.0% is mainly due to an increase in base rates granted by the Pennsylvania Public Utility Commission, effective September 1, 1978, which resulted in a 21.9% base rate increase. On July 1, 1978, the Company rolled 95% of the energy costs for the 12-month period ended July 31, 1977 into base rates as a result of a Pennsylvania Public Utility Commission Order. Surcharge revenues increased 34.1% and kilowatt-hour sales increased 2.9%.

Since September 1977, the Company has been collecting rates subject to refund from the municipal resale class pending a decision by the Federal Energy Regulatory Commission. The 1979 revenues have been adjusted to exclude an estimated $1,023,923 which is the amount estimated to be refundable to the municipal resale customers for this 28-month period.

Operating and Maintenance Expenses—

The increase in 1978 of $12,739,000 reflects an increase of $2.89 in the cost per ton of coal consumed, as well as the fact that kilowatt-hours generated from Beaver Valley Unit No. 1 (Nuclear) decreased 7.4% while kilowatt-hours generated from oil combustion units increased 43.1%. Also contributing to the increase in operating costs was the placing in commercial operation of Bruce Mansfield Unit No. 2 in October 1977, thus reflecting a full year of expenses. Purchased and interchanged power increased due to the Company's buy/sell position as a member of CAPCO caused by extended outages of various CAPCO units, which put the Company in a "Net Receipt" position.

The increase in 1979 of $11,923,000 reflects an increase of $3.58 in the cost per ton of coal consumed along with a minimal increase in tons consumed and kilowatt-hours generated. This increase is partially offset by a 38.9% decrease in kilowatt-hours generated from oil combustion units. The overall kilowatt-hours generated from all units decreased 125,347,100 or 3.8% while the cost of fuel consumed for all units increased $4,117,290 or 10.4%. Also contributing to the overall increase in cost of fuel is an increase of $2,862,000 due to the operation of the Company's deferred energy clause. Purchased and interchanged power increased $4,382,000 or 139.8% in 1979 over 1978 due to a reduction in kilowatt-hour deliveries to the parent, Ohio Edison Company, in 1979 compared to 1978 when Ohio Edison Company received substantial deliveries from Pennsylvania Power Company as a result of a coal strike during the first quarter of 1978. In addition, the Company sold fewer kilowatt-hours to other CAPCO companies during 1979 as a result of a change in our buy/sell position and the unavailability of the Beaver Valley Nuclear Unit caused by a Nuclear Regulatory Commission Order.

In 1978 maintenance expenses increased due to replacement of a failed step-up transformer at Beaver Valley Unit No. 1, replacement of a generator at W. H. Sammis Unit No. 7, along with forced and scheduled outages of various units at the New Castle Power Plant during the year. The forced outages at Beaver Valley Unit No. 1 and W. H. Sammis Unit No. 7 together entailed nearly a year of downtime. Maintenance expenses in 1979 increased principally due to scheduled outages at the New Castle Power Plant and W. H. Sammis Unit No. 7. The No. 5 Unit at the New Castle Power Plant was down approximately four months for a boiler and turbine overhaul. Escalating wage and fringe benefits, increased material and other costs also contributed to the overall rise in the level of expenses.

Depreciation–
The provision for depreciation increased $1,233,000 for the year 1978 due to placing in service Bruce Mansfield Unit No. 2 in October 1977 and other additional property. The 1978 increase was partially offset by the adoption of reduced depreciation rates approved by the Pennsylvania Public Utility Commission. The increase of $630,000 in 1979 is due to additional plant placed in service.

Taxes–
General taxes increased $1,199,000 for the year 1978 and $2,380,000 for the year 1979. The 1978 increase reflects higher gross receipts taxes as a result of higher revenues, and additions to property have resulted in higher property taxes. The 1979 increase in general taxes is principally due to an increase in Pennsylvania Gross Receipts Tax resulting from an increase in rates granted by the Pennsylvania Public Utility Commission effective September 1, 1978 and an increase in the Pennsylvania Public Utility Realty Tax due to an expanded tax base at the 30 mill rate and a one-time surtax at 105 mills upon the taxable value of items of utility realty at December 31, 1978 previously excluded from the tax base less amounts of petitions for refunds of the realty tax paid in prior years.

Changes in the provisions for income taxes for the years 1978 and 1979 are set forth in Note 1 of Notes to the Financial Statements.

Other Income (Net)–
The decrease in 1978 of $542,000 results principally from the decrease in allowance for funds used during construction, reflecting the placing in commercial operation of Bruce Mansfield Unit No. 2 in October 1977, although the overall rate for computing the allowance was increased slightly. The increase in 1979 of $1,487,000 reflects a higher level of construction work in progress.

Net Interest–
The increase in 1978 of $3,256,000 reflects the sale of first mortgage bonds in April 1978, and a decrease in allowance for borrowed funds used during construction, a credit amount, due to the placing in commercial operation of Bruce Mansfield Unit No. 2 in October 1977. The 1979 increase of $934,000 reflects the sale of pollution control notes and first mortgage bonds in April and June of 1979, respectively, and the increase in short-term borrowings. The above increase is partially offset by the allowance for borrowed funds used during construction, a credit amount, due to the increase in the level of construction work in progress.

Pennsylvania Power Company

STATEMENTS OF INCOME AND RETAINED EARNINGS: For the Years Ended December 31, 1979 and 1978

	1979	1978	Increase or Decrease
		Thousands of Dollars	
Electric Operating Revenues (Note 1)	$145,340	$119,118	+$ 26,222
Operating Expenses and Taxes:			
Operation—			
Cost of fuel (Note 1)	45,587	38,608	+ 6,979
Purchased and interchanged power, net (Note 1)	7,516	3,134	+ 4,382
Other operation expenses	19,204	19,483	– 279
Total operation	72,307	61,225	+ 11,082
Maintenance	13,423	12,582	+ 841
Provision for depreciation (Note 1)	12,517	11,887	+ 630
General taxes	10,296	7,916	+ 2,380
Income taxes (Note 1)	7,376	1,753	+ 5,623
Total operating expenses and taxes	115,919	95,363	+ 20,556
Operating Income	29,421	23,755	+ 5,666
Other Income and Deductions:			
Allowance for equity funds used during construction (Note 1)	6,258	4,592	+ 1,666
Miscellaneous, net	78	419	– 341
Income taxes (Note 1)	(39)	(201)	+ 162
Total other income and deductions, net	6,297	4,810	+ 1,487
Total Income	35,718	28,565	+ 7,153
Net Interest:			
Interest on long-term debt	17,353	15,292	+ 2,061
Allowance for borrowed funds used during construction (Note 1)	(4,301)	(2,613)	– 1,688
Other	1,460	899	+ 561
Net interest	14,512	13,578	+ 934
Net Income	21,206	14,987	+ 6,219
Preferred Stock Dividend Requirements	4,660	4,660	–
Net Income for Common Stock	$ 16,546	$ 10,327	+$ 6,219
Retained Earnings—Balance at beginning of year	$ 32,828	$ 28,139	+$ 4,689
Net income for common stock	16,546	10,327	+ 6,219
Less—Dividends on common stock	12,278	5,452	+ 6,826
—Dividends declared on preferred stock in excess of current period's requirements	–	174	– 174
Capital stock issuance expense	–	12	– 12
Retained Earnings—Balance at end of year (Note 5)	$ 37,096	$ 32,828	+$ 4,268

( ) Denotes negative amount

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

Pennsylvania Power Company

Balance Sheets: at December 31, 1979 and 1978

Assets

	1979	1978	Increase or Decrease
		Thousands of Dollars	
Utility Plant (Note 1):			
In service, at original cost	$429,016	$414,657	+$ 14,359
Less—Accumulated provision for depreciation	101,585	90,742	+ 10,843
	327,431	323,915	+ 3,516
Construction work in progress	115,989	90,126	+ 25,863
Nuclear fuel in process	1,739	1,591	+ 148
	445,159	415,632	+ 29,527
Other Property and Investments:			
Construction funds held in escrow, including accrued interest	76	2,200	− 2,124
Other, at cost	313	313	−
	389	2,513	− 2,124
Current Assets:			
Cash	1,429	795	+ 634
Receivables—			
Customers (less accumulated provision of $180,000 and $160,000, respectively, for uncollectable accounts)	11,372	11,221	+ 151
Parent Company	8,661	10,373	− 1,712
Other	7,786	9,228	− 1,442
Materials and supplies, at average cost—			
Fuel	9,745	8,138	+ 1,607
Other	4,146	3,323	+ 823
Prepayments and other	617	484	+ 133
	43,756	43,562	+ 194
Deferred Debits:			
Deferred energy costs (Note 1)	3,030	4,717	− 1,687
Deferred cost of terminated construction projects (Note 3)	14,761	−	+ 14,761
Other	10,190	7,423	+ 2,767
	27,981	12,140	+ 15,841
	$517,285	$473,847	+$ 43,438

The accompanying Notes to Financial Statements are an integral part of these balance sheets.

Capitalization and Liabilities

	1979	1978	Increase or Decrease
		Thousands of Dollars	
Capitalization: (See Statements of Capitalization)			
Common stockholder's equity	$154,396	$150,128	+$ 4,268
Non-redeemable preferred stock	41,947	41,947	–
Redeemable preferred stock	17,600	18,000	– 400
Long-term debt	225,156	205,683	+ 19,473
	439,099	415,758	+ 23,341
Current Liabilities:			
Current maturities of long-term debt and preferred stock	3,400	–	+ 3,400
Notes payable to banks (Note 6)	15,500	6,500	+ 9,000
Accounts payable–			
Parent Company	2,503	1,971	+ 532
Other	23,675	23,362	+ 313
Accrued taxes	6,306	3,329	+ 2,977
Accrued interest	3,483	3,219	+ 264
Dividends declared on preferred stock	934	934	–
Miscellaneous	2,321	1,872	+ 449
	58,122	41,187	+ 16,935
Deferred Credits:			
Accumulated deferred income taxes (Note 1)	10,139	9,853	+ 286
Accumulated deferred investment tax credits (Note 1)	5,242	2,608	+ 2,634
Other	4,683	4,441	+ 242
	20,064	16,902	+ 3,162
Commitments, Guarantees and Contingencies (Notes 2, 4 and 7)			
	$517,285	$473,847	+$ 43,438

The accompanying Notes to Financial Statements are an integral part of these balance sheets.

Pennsylvania Power Company

Statements of Capitalization: at December 31, 1979 and 1978

	Number of Shares Outstanding 1979	Number of Shares Outstanding 1978	Optional Redemption Price Per Share	Optional Redemption Price Aggregate (In Thousands)	1979 (Thousands of Dollars)		1978 (Thousands of Dollars)	
Common stockholder's equity:								
Common stock, $30 par value, authorized—4,800,000 shares—outstanding 3,910,000 shares					$117,300		$117,300	
Retained earnings (Note 5a)					37,096		32,828	
Total common stockholder's equity					154,396	35.2%	150,128	36.1%
Preferred stock (Note 5b):								
Cumulative, $100 par value								
Authorized—740,000 shares, issuable in series								
Non-redeemable:								
4.24% - 4.64%	141,049	141,049	$102.980-105.000	$14,614	14,105		14,105	
7.64% - 8.00%	118,000	118,000	106.380-107.270	12,605	11,800		11,800	
8.48% - 9.16%	160,000	160,000	107.320-109.160	17,319	16,000		16,000	
Premium	—	—		—	42		42	
Total non-redeemable preferred stock	419,049	419,049		$44,538	41,947	9.5	41,947	10.1
Redeemable (Note 5c):								
8.24%	100,000	100,000	$108.240	$10,824	10,000		10,000	
11.00%	80,000	80,000	112.110	8,969	8,000		8,000	
	180,000	180,000		$19,793	18,000		18,000	
Redeemable within one year					(400)		—	
Total redeemable preferred stock					17,600	4.0	18,000	4.3
Long-term debt (Note 5d):								
First mortgage bonds—								
2-3/4% Series due 1980					—		3,000	
9-5/8% Series due 1981					5,000		5,000	
3-1/4% Series due 1982					5,805		5,805	
9-1/2% Series due 1985					25,000		25,000	
4-3/8% - 10-1/2% Series due 1992 through 2000					68,000		48,000	
7-5/8% - 9-1/2% Series due 2001 through 2008					74,000		74,000	
Total first mortgage bonds					177,805		160,805	
Secured notes and obligation—								
Pollution control—								
1973 Series A, average interest rate 5.75%, due 1984 through 2003					3,500		3,500	
1974 8-3/8% Series A and B, due 1990 through 2004					6,547		6,547	
1976 7-7/8% - 8% Series A and D, due 1992 through 2006					20,000		20,000	
1977 4-3/4% Series E, due 1979 (refinanced in 1979)					—		3,500	
1977 6-3/4% Series B, due 1998 through 2007					10,600		10,600	
1978 7.30% Obligation, due 1988 through 2003					314		314	
1979 7.80% Series C and F, due 2004					6,000		—	
					46,961		44,461	
1976 7.90% Environmental Note, due 1992 through 2001					1,000		1,000	
Total secured notes and obligation					47,961		45,461	
Net unamortized premium (discount) on debt					(610)		(583)	
Total long-term debt					225,156	51.3	205,683	49.5
Total capitalization (Note 7)					$439,099	100.0%	$415,758	100.0%

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

Pennsylvania Power Company

Statements of Sources of Funds for Gross Property Additions:

For the Years Ended December 31, 1979 and 1978

	1979	1978
	Thousands of Dollars	
Sources of Funds:		
Net income	$ 21,206	$ 14,987
Less—Dividends on common stock	12,278	5,452
Dividends on preferred stock	4,660	4,834
	4,268	4,701
Principal non-cash items—		
Depreciation and amortization—		
Charged to provision for depreciation	12,517	11,887
Charged to other accounts	201	199
Deferred income taxes—net	3,382	2,801
Investment tax credits—net	2,634	(1,458)
Allowance for equity funds used during construction	(6,258)	(4,592)
Deferred energy costs, net of deferred income taxes (increase) decrease	806	(624)
Total funds from operations	17,550	12,914
Proceeds from issuance of—		
Common stock	–	4,500
First mortgage bonds	20,000	25,000
Secured notes and obligation	6,000	314
Increase in notes payable to banks	9,000	6,500
	35,000	36,314
Payment at maturity of long-term debt	(3,500)	(1,000)
Construction funds held in escrow including accrued interest	2,124	5,540
Net change in current assets and current liabilities excluding notes payable to banks and current maturities of long-term debt and preferred stock—		
Receivables	3,003	(13,216)
Materials and supplies	(2,430)	(616)
Accounts payable	845	12,731
Accrued taxes	2,977	(360)
Other, net	(54)	523
	4,341	(938)
Other, net (i)	2,161	2,128
Gross Property Additions (i)	$ 57,676	$ 54,958

( ) Denotes negative amount

(i) Includes allowance for equity funds used during construction (Note 1).

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

Notes to Financial Statements:

(1) Summary of Accounting Policies:

The Company follows the accounting policies and practices prescribed by the Pennsylvania Public Utility Commission (the Commission) and the Federal Energy Regulatory Commission (FERC). The more significant policies are summarized below.

Revenues–

The Company's residential and commercial customers are metered on a cycle basis. The Company's policy is to include in revenue residential and commercial service revenues relating to meters read through the end of the month.

Effective September 11, 1977, the FERC authorized the Company to increase its rates for municipal resale service to yield approximately $1,317,000 of additional annual revenues based on the test year data. The approved rates are being collected subject to refund pending the results of further hearings. For each of the years 1979 and 1978, operating revenues and net income, attributable to such rate increase, amount to approximately $1,500,000 and $475,000, respectively. Management believes that any refunds which may be required in this case would not have a significant effect on the results of operations for the periods presented.

Revenues attributed to the Company's largest customer amounted to approximately $17,465,000 and $14,200,000 for 1979 and 1978, respectively, which represented approximately 12.0% of the Company's total operating revenues in each year.

Deferred Energy Costs–

The Company defers certain increased energy costs incurred and estimated to be billable to most customers in succeeding periods in accordance with its energy clause. Effective July 1, 1978, the Commission adopted an energy clause which replaced the fuel adjustment clause. The energy clause provides for the recovery or refund, over a six-month period, which commences two calendar months after incurrence, of energy costs which differ from established base energy costs. The energy clause also provides for an adjustment for any over or under collection resulting from the operation of this clause.

The effect of the Company's accounting, which has been approved by the Commission, was to decrease net income for 1979 by $806,000, and to increase net income for 1978 by $624,000.

Management expects that the Commission will allow the Company full recovery of any deferred costs including those relating to changes in the lag period or any other changes, in accordance with the objectives of the energy clause provisions included in its approved tariffs.

Utility Plant, Depreciation and Maintenance–

Utility plant is stated at the original cost of construction which includes payroll and related costs such as taxes, pensions and other fringe benefits, general and administrative costs and an allowance for funds used during construction (see Allowance for Funds Used During Construction).

The Company provides for the depreciation of depreciable plant in service on a straight-line basis at various rates over the estimated lives of the property. In the opinion of management, the amounts provided have been adequate and the methods used to determine the amounts meet the requirements of the regulatory commissions. The effective annual composite rate for 1979 and 1978 is approximately 3.1%. The Company was granted a total allowance of approximately $2,300,000 for its share of the estimated decommissioning costs of the radioactive components of its only nuclear generating unit in service in its recent rate case and began providing for such costs in 1979.

Property additions, renewals and replacements are charged to utility plant accounts. Property considered to be retirement units, retired or otherwise disposed of in the normal course of business, together with the cost of removal, less salvage, is charged to the accumulated provision for depreciation and no gain or loss is recognized in the income accounts. Repairs of property are charged to maintenance.

Common Ownership of Generating Facilities–

The Company and other Central Area Power Coordination (CAPCO) group companies own various power generating facilities as tenants in common. Each of the companies is obligated to pay a share of the costs of any such jointly owned facilities in the same proportion as its ownership interest therein. The amounts reflected in the accompanying Balance Sheet under utility plant include such costs at December 31, 1979 as follows:

	CAPCO Units in Service (b)			CAPCO Units under Construction		
	W. H. Sammis 7	Bruce Mansfield 1 and 2	Beaver Valley 1	Bruce Mansfield 3	Perry 1 and 2	Total
			Thousands of Dollars			
Utility plant in service	$ 25,113	$ 45,181(a)	$101,749	$ –	$ –	$172,043
Accumulated provision for depreciation	$ 5,343	$ 3,535	$ 10,185	$ –	$ –	$ 19,063
Construction work in progress	$ 347	$ 1,441	$ 8,537	$ 27,466	$ 71,191	$108,982
Nuclear fuel in process (c)						$ 1,739
Company's ownership interest in unit capacity	20.8%	5.5%	17.5%	6.28%	6.28%	

(a) Includes common facilities.

(b) The Company's portion of operating expenses associated with the common ownership of generating facilities is included in the corresponding operating expenses in the accompanying Statements of Income.

(c) Unsegregated amount among the CAPCO nuclear units.

Nuclear Fuel—

The cost of nuclear fuel in service is charged to fuel expense based on the rate of consumption assuming a zero net salvage value. The manner of disposition of spent nuclear fuel may not be determined for many years, therefore necessitating storage of such fuel for an indefinite period. The Company will seek regulatory approval for recovery of such costs through its rate case proceedings.

Allowance for Funds Used During Construction—

The allowance for funds used during construction, a non-cash item which is charged to construction work in progress during the period of construction, represents the net cost of borrowed and equity funds used for construction purposes. The amount of the allowance varies as a result of changes in the level of construction work in progress and in the sources of capital. The Company computes the allowance utilizing a net of tax rate consistent with its rate treatment. The rate used during 1979 and 1978 was 8%.

Income Taxes—

The provision for income taxes shown in the accompanying Statements of Income consists of the following components:

	1979	1978
	Thousands of Dollars	
Currently payable—		
Federal	$ 1,330	$ –
State	950	59
Total currently payable	2,280	59
Deferred, net—		
Federal	1,893	2,880
State	608	473
Total deferred, net (see below)	2,501	3,353
Investment tax credits, net of amortization (i)	2,634	(1,458)
Total provision for income taxes	$ 7,415	$ 1,954

( ) Denotes negative amount

(i) 1978 reflects the reversal of previously recorded investment tax credits, now being carried forward due to the carry-back of net operating losses.

Such provision is included in the accompanying Statements of Income as follows:

	1979	1978
	Thousands of Dollars	
Operating Expenses	$ 7,376	$ 1,753
Other Income	39	201
Total provision for income taxes	$ 7,415	$ 1,954

Deferred tax expense results from timing differences in the recognition of revenues and expenses for tax and accounting purposes. The sources of these differences and tax effect of each are as indicated below:

	1979	1978
	Thousands of Dollars	
Debt component of allowance for funds used during construction which is credited to plant	$ 2,215	$ 1,392
Excess of tax depreciation allowed pursuant to the Class Life ADR depreciation system, net	1,309	1,599
Accelerated amortization of the cost of certain facilities covered by Necessity Certificates	(182)	(182)
Property taxes applicable to subsequent periods, net	40	(8)
	3,382	2,801
Deferred energy costs, net	(881)	552
Total deferred tax expense, net	$ 2,501	$ 3,353

( ) Denotes negative amount

For income tax purposes, the Company has claimed liberalized depreciation (double-declining balance, guideline lives and the Class Life ADR System provision methods) and, consistent with the accounting and rate-making policies of the applicable regulatory authorities, the Company has followed "flow-through" accounting except as indicated above.

The Company follows deferral accounting with respect to investment tax credits and amortizes such credits to income over the estimated life of the related property. At December 31, 1979, approximately $12,000,000 of unused investment tax credits were available to offset future Federal income taxes payable, of which $4,000,000 expires at the end of 1983, $4,000,000 expires at the end of 1984, $3,000,000 expires at the end of 1985 and $1,000,000 expires at the end of 1986.

The total provision for income taxes shown in the accompanying Statements of Income is less than the amount which would be computed by applying the statutory Federal income tax rate to income before income taxes. The following table summarizes the major reasons for these differences:

	1979	1978
	Thousands of Dollars	
Book income before provision for income taxes	$28,621	$16,941
Amount of Federal income tax expense at statutory rate	$13,166	$ 8,132
Increases (reductions) in taxes resulting from: (i)		
Allowance for equity funds used during construction which does not constitute taxable income	(2,879)	(2,204)
Excess of tax over book depreciation	(3,296)	(3,837)
State income taxes, net of Federal income tax benefit	841	277
Capitalized overhead costs	254	(105)
Amortization of deferred investment tax credits	(376)	66
Other, net	(295)	(375)
Total provision for income taxes	$ 7,415	$ 1,954

( ) Denotes negative amount

(i) Under the established rate-making practices of the regulatory commissions to which the Company is subject, it is expected that the deferred taxes not provided for currently will be collected in customers' rates when such taxes become payable.

It is not expected that the cash outlay for income taxes with respect to any of the succeeding three years will materially exceed income tax expense for such years.

Pensions—

The Company has a trusteed noncontributory pension plan covering substantially all full-time employees. Upon retirement, employees are provided a monthly pension based on length of service and compensation. Pension costs for 1979 and 1978 were $2,321,000 and $1,949,000, respectively, of which $1,146,000 and $899,000, respectively, were charged to operating expenses and the balances were charged primarily to construction. Such costs include the amortization of past service costs on an actuarial basis over 30 years. The Company funds pension costs accrued. The estimated unfunded past service liability of the plan at June 30, 1979 (the date of the latest actuarial report) was $7,715,000. The market value of the pension fund at December 31, 1979 exceeded the actuarially computed value of the vested benefits at June 30, 1979.

Purchased and Interchanged Power, Net—

Purchased and interchanged power, net in the accompanying Statements of Income includes the interchange of power with Ohio Edison Company, the Company's parent, which resulted in a net expense to the Company of $7,600,000 in 1979 and $4,500,000 in 1978. Such amounts are determined in accordance with operating agreements entered into by the Company with the CAPCO companies. These agreements prescribe the method of accounting to be followed in the billing of power, and have been filed with the FERC.

(2) Ohio Valley Electric Corporation (OVEC):

The Company and Ohio Edison Company are participating with 13 other investor-owned electric utility companies and with OVEC in arrangements with the Department of Energy (DOE) to supply the power requirements of the DOE plant near Portsmouth, Ohio. The sponsors are entitled to receive from OVEC, and are obligated to pay for the right to receive, any available power in excess of the DOE contract demand. The proceeds from the sale of power by OVEC are to be sufficient to meet all of its costs including amortization of debt capital over a period ending December 31, 1981, and to provide for a return on common stock. At December 31, 1979, OVEC had debt capital of approximately $24,000,000 remaining to be amortized. The participation of the Company in the power arrangements is 2%.

(3) Terminated Construction Projects:

In January 1980, the Company and all other CAPCO companies terminated plans to construct the following four nuclear generating units—Davis-Besse No. 2 and No. 3, and Erie No. 1 and No. 2. The Company's share of construction costs incurred as of December 31, 1979 applicable to these units amounted to $14,761,000. The Company intends to seek approval from the Commission and the FERC to amortize these amounts plus contractors' cancellation charges, if any, over several years and to recover the costs from customers to the extent that they are not otherwise recoverable. The Company believes that such costs were prudently incurred and has no reason to believe that the regulatory authorities involved will not react favorably to its requests and therefore believes that any loss of investment and cancellation charges, if any, will be recoverable from its customers. Until orders are received from the Commission and the FERC, none of the charges will be reflected in earnings.

(4) Leases:

The Company rents or leases nuclear fuel, certain transmission and distribution facilities, office space and other incidental equipment and property under cancelable and noncancelable leases. The total rent expense included in the accompanying Statements of Income for 1979 and 1978 was $2,304,000 and $3,109,000, respectively. The future minimum rental commitments as of December 31, 1979 for all noncancelable leases are as follows:

1980	$ 2,290,000
1981	3,968,000
1982	4,125,000
1983	3,627,000
1984	2,402,000
1985 - 2023	43,687,000

If all noncapitalized financing leases had been capitalized, the effect on total assets, total liabilities and expenses would not be material.

(5) Capitalization:

(a) Retained Earnings—

Under the Company's indenture, the Company's retained earnings not available for payment of cash dividends on the Company's Common Stock was $13,124,000 at December 31, 1979.

(b) Preferred Stock—

The Company had 140,951 shares of preferred stock authorized and unissued at December 31, 1979.

The preferred stock is redeemable in whole or in part, unless otherwise noted, at the option of the Company, at any time upon not less than 30 nor more than 60 days notice.

Redemption of preferred stock (excluding the 4.24% – 4.64% Series) is subject to certain restrictions regarding refunding operations for five years from date of issue. The current redemption prices shown will decline to eventual minimums per share in accordance with the Charter provisions establishing each series.

(c) Redeemable Preferred Stock–

The 11% Series includes a provision for a mandatory sinking fund sufficient to retire a minimum of 4,000 shares at $100 per share plus accrued dividends on January 1 in each year beginning in 1980. The 8.24% Series includes a provision for a mandatory sinking fund sufficient to retire a minimum of 5,000 shares at $100 per share plus accrued dividends on December 1 in each year beginning in 1982.

The sinking fund requirements for each of the five years ending December 31, 1980 through 1984 will amount to:

1980	$400,000
1981	400,000
1982	900,000
1983	900,000
1984	900,000

(d) Long-Term Debt–

Substantially all property owned by the Company is subject to a direct first mortgage lien.

Based on the amount of bonds authenticated by the trustee through December 31, 1979, the annual sinking and improvement fund requirements amount to $2,019,000. It is presently contemplated that these requirements will be satisfied in 1980 by permanently waiving the Company's right to issue bonds against $2,019,000 of the $2,798,000 of retired bonds that are presently available for that purpose. In the alternative, the Company could deposit funds in the amount called for which could then be withdrawn upon surrender for cancellation of a like principal amount of bonds specifically authenticated for such purposes against unfunded property additions. The withdrawal of sinking and improvement fund deposits in this manner results in a minor increase in the amount of the annual sinking and improvement fund requirements for the Company.

As of December 31, 1979, the sinking and improvement fund requirements and maturities of long-term debt for each of the five years ending December 31, 1980 through 1984 will amount to:

1980	$5,019,000
1981	7,019,000
1982	7,824,000
1983	2,019,000
1984	2,069,000

(6) Notes Payable to Banks and Lines of Credit:

The Company has lines of credit that provide for borrowings of up to $20,000,000 at rates varying from prime to 108% of the prevailing prime interest rates. Short-term borrowings may be made under these lines of credit on unsecured notes of the Company. All of the current lines expire December 31, 1980; however, all unused lines are cancelable at the option of the banks.

The Company maintains cash balances on deposit with the bank to provide operating funds and to assure availability of $4,500,000 of the above-mentioned lines of credit. Such compensating balances, net of "float", are expected to be maintained at an average of $320,000. These balances are not subject to any contractual restriction against withdrawal. In addition, the Company is required to pay a commitment fee to assure the availability of an additional $4,500,000 of the above-mentioned lines of credit.

Additional information with respect to these notes payable is as follows:

	1979	1978
Interest rate on outstanding bank line borrowings at December 31	15.14%	11.75%
Maximum amount drawn down during the year	$19,500,000	$12,000,000
Average borrowings during the year	$ 8,083,000	$ 2,913,000
Weighted average interest rate during the year (based on the daily amounts outstanding–excluding commitment fee)	12.98%	10.16%

(7) Commitments, Guarantees and Contingencies:

The currently estimated cost of property additions and improvements presently expected to be required by the Company during the period 1980-1984, inclusive, is approximately $251,481,000 of which $59,600,000 is applicable to the year 1980. The major portion of the Company's construction activities during the 1980-1984 period relates to the CAPCO companies' program for the joint development of power generation and transmission facilities. In connection with the future commercial operation of nuclear generating units, the CAPCO companies have entered into commitments with respect to the supply of nuclear fuel. The Company's share of the cost associated with such commitments is estimated to be $230,000,000.

The Company presently contemplates a financing program during this five-year period which will include the sale or issuance from time to time of appropriate additional amounts of first mortgage bonds, secured pollution control and environmental notes and obligations, preferred stock and common stock. The issuance of additional first mortgage bonds and preferred stock is subject to the limitation requirements of the Company's mortgage indenture and charter.

The Company, together with the other CAPCO companies, has made long-term coal supply arrangements with Quarto Mining Company (Quarto). The CAPCO companies have severally, and not jointly, agreed to guarantee their proportionate shares of Quarto's debt and lease obligations incurred in connection with developing and equipping the mines whether or not the coal can be utilized because of environmental considerations. As of December 31, 1979, the Company's share of the guarantee was $30,702,000 ($11,619,000—long-term indebtedness, $11,681,000—lease obligations and $7,402,000—short-term bank credit), which is ultimately expected to increase to $35,640,000 based on presently budgeted mine construction costs of $431,000,000. Because of significant difficulties experienced during the development period, the CAPCO companies are reviewing the various alternatives available to reduce unit production costs, which are presently in excess of the current spot market price of coal. Management believes that the costs incurred in connection with this project will be recovered through the operation of the Company's energy clause or through base rates.

The Company is subject to regulation with regard to air and water quality and other environmental matters by various Federal, state and local authorities. For compliance therewith, it is presently estimated that additional capital expenditures of approximately $61,000,000 may be required by the Company, of which approximately $26,000,000 has been expended prior to 1980 and $24,000,000 is included in the estimated construction costs for the 1980-1984 period referred to above. If the use of low sulfur non-Ohio coal is not permitted for compliance with Federal sulfur dioxide emission limitations at Sammis Unit No. 7, estimated capital expenditures would be increased by approximately $26,000,000 and annual operating costs would be increased substantially. Similarly, if a flue gas desulfurization device must be installed at the Company's New Castle plant to comply with such emission limitations, it is estimated that the capital expenditures would be increased by $85,000,000 and annual operating expenses would increase by approximately $15,000,000. If the Company is required to install additional off-stream cooling in connection with the operation of the New Castle plant and W. H. Sammis Unit No. 7, additional substantial but presently undeterminable costs would be incurred. Although the Company is unable to predict the ultimate results of the legal proceedings pending in Ohio and Pennsylvania relating to compliance with environmental regulations or any additional capital and operating expenditures that may be necessary as a result thereof, it expects that the impact of any such costs eventually would be reflected in its rate schedules.

In some proceedings, criminal fines or civil penalties ultimately could be imposed under the Clean Air Act Amendments of 1977 and the Federal Water Pollution Control Act as amended by the Clean Water Act of 1977 or the Company could be forced to shut down significant amounts of coal-fired capacity. The Federal government has begun legal proceedings against the Company under the Clean Air Act asking the courts to assess civil penalties for alleged continuing violations of particulate emission regulations at the W. H. Sammis Plant and sulfur dioxide emission regulations at the Company's New Castle Power Plant. The Clean Air Act amendments which became effective in August, 1977, permit the imposition of civil penalties of up to $25,000 per day of violation. The penalties, if any, that may be imposed by the courts for alleged past violations are not now determinable, but such penalties could be substantial. Ohio Edison, the operator of the Sammis Plant, and the Company expect to comply with any final orders of the courts and in the meantime to conduct the operation of the plants so as to minimize the applicable emissions to the greatest extent that they deem to be practicable; therefore, the litigation described above should not result in the imposition of any substantial civil penalties for future conduct.

The Federal Environmental Protection Agency (EPA) had tentatively indicated an intention to seek to enforce noncompliance penalties beginning August 7, 1979, for failure to comply with applicable emission limits, as required under the Clean Air Act; however, final regulations have not been issued. Even if the application to change the State Implementation Plan which would bring the New Castle Power Plant into compliance and the submitted schedule to bring the Sammis Plant into compliance by 1984 are accepted, substantial noncompliance penalties may result. Until final regulations are issued, the date from which penalties will begin and the method of calculating such penalties will not be known.

In addition, the following summarizes certain other outstanding legal actions and complaints against the Company:

In 1977, the Borough of Shippingport, Pennsylvania, filed actions against the CAPCO companies seeking to enjoin the operation of the Bruce Mansfield and Beaver Valley plants and to obtain damages resulting from alleged operational malfunctions of the flue gas desulfurization system at Mansfield and the threat of radioactive emissions at Beaver Valley. In addition, numerous individual plaintiffs have filed actions seeking monetary relief in an unspecified amount for damages claimed to be the result of the same alleged operational malfunctions. Although unable to predict the ultimate outcome of the matter, the Company believes that the ultimate disposition will not result in any material adverse effect on the Company's financial position and results of operations.

In 1977, the Boroughs of Ellwood City and Grove City, Pennsylvania, filed a complaint against the Company, alleging that the Company, individually and in conspiracy with Ohio Edison and other CAPCO companies, has violated Sections 4 and 16 of the Clayton Act to restrain and monopolize trade and commerce in alleged markets for electric power. Damages of $7,000,000 (to be trebled) and injunctions against the unlawful acts are sought. On January 4, 1979, the Court granted summary judgment in favor of the Company as to certain allegations of the complaint. Management is unable to predict the ultimate outcome of this action.

On April 10, 1979, Kerr-McGee Nuclear Corporation filed a complaint against the CAPCO companies alleging a breach of a 1973 uranium supply contract, thus allegedly entitling Kerr-McGee to treat the contract as having been terminated. Kerr-McGee also seeks unspecified damages, costs and such further relief as the Court deems just and proper. If the uranium is not delivered by Kerr-McGee, steps will have to be taken to effect other arrangements, which may result in additional but presently undeterminable costs to CAPCO members. On June 28, 1979, the CAPCO members filed a counteraction against Kerr-McGee Corporation and Kerr-McGee Nuclear Corporation seeking a declaration by the Court as to the rights of the parties and a granting by the Court of the plaintiffs' costs and exemplary damages due to defendants' attempt to extract price increases from the plaintiffs.

The Commission instituted an investigation into an outage of Beaver Valley Unit No. 1 during the period March-August 1979, which outage had been ordered by the Nuclear Regulatory Commission to analyze possible seismic deficiencies of safety-related piping and pipe supports in the Unit. This investigation is to determine whether, as a result of this outage, the Unit should be eliminated from, or adjustments should be made in, the Company's rate base and whether expenditures by the Company for purchased replacement power should be disallowed for purposes of the Company's energy clause. In a separate investigation, the Commission is considering whether additional construction costs resulting from deferral of construction projects should be excluded from rate base in subsequent rate proceedings.

(8) Summary of Quarterly Financial Data:

The following data summarize certain operating results for the four quarters of 1979 and 1978.

	Three Months Ended			
	March 31, 1979	June 30, 1979	September 30, 1979	December 31, 1979
	Thousands of Dollars			
Operating Revenues	$37,335	$35,444	$36,595	$35,966
Operating Expenses and Taxes	29,496	29,080	28,367	28,976
Operating Income	7,839	6,364	8,228	6,990
Other Income and Deductions, net	1,368	1,510	1,646	1,773
Net Interest	3,355	3,592	3,717	3,848
Net Income	$ 5,852	$ 4,282	$ 6,157	$ 4,915
Net Income for Common Stock	$ 4,687	$ 3,117	$ 4,992	$ 3,750

	Three Months Ended			
	March 31, 1978	June 30, 1978	September 30, 1978	December 31, 1978
	Thousands of Dollars			
Operating Revenues	$27,305	$26,352	$29,556	$35,905
Operating Expenses and Taxes	21,334	21,141	24,471	28,417
Operating Income	5,971	5,211	5,085	7,488
Other Income and Deductions, net	857	1,282	1,163	1,508
Net Interest	3,026	3,300	3,457	3,795
Net Income	$ 3,802	$ 3,193	$ 2,791	$ 5,201
Net Income for Common Stock	$ 2,637	$ 2,028	$ 1,626	$ 4,036

Auditors' Report

ARTHUR ANDERSEN & CO.

1345 AVENUE OF THE AMERICAS
NEW YORK, N.Y. 10019

To the Board of Directors of Pennsylvania Power Company:

We have examined the balance sheets and statements of capitalization of Pennsylvania Power Company (a Pennsylvania corporation and a wholly-owned subsidiary of Ohio Edison Company) as of December 31, 1979, and 1978, and the related statements of income and retained earnings and sources of funds for gross property additions for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Pennsylvania Power Company as of December 31, 1979, and 1978, and the results of its operations and sources of funds for gross property additions for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

February 8, 1980

Arthur Andersen & Co.

PENNSYLVANIA POWER COMPANY
Supplementary Financial Data
Financial Reporting and Changing Prices

Statement of Financial Accounting Standards No. 33, "Financial Reporting and Changing Prices" (SFAS No. 33), provides for the preparation of supplementary financial information to disclose the estimated effects of inflation and changes in prices on property, plant and equipment. This data is presented in accordance with SFAS No. 33, however, it is not intended as a substitute for earnings reported on a historical cost basis.

Adjusted for the Effects of Changing Prices For the Year Ended December 31, 1979 (In Thousands)	**As Reported in the Primary Statements**	**Historical Cost Adjusted for General Inflation**	**Adjusted for Change in Specific Prices (Current Cost)**
		(Average 1979 Dollars)	
Operating Revenues	$145,340	$145,340	$145,340
Operating Expenses and Taxes:			
Operation and maintenance	85,730	85,730	85,730
Provision for depreciation	12,517	22,373	24,123
General taxes	10,296	10,296	10,296
Income taxes	7,376	7,376	7,376
Total operating expenses and taxes	115,919	125,775	127,525
Operating Income	29,421	19,565	17,815
Other Income and Deductions, net	6,297	6,297	6,297
Net Interest	14,512	14,512	14,512
Preferred Stock Dividend Requirements	4,660	4,660	4,660
Income from Continuing Operations (excluding reduction to net recoverable cost)	$ 16,546	$ 6,690(a)	$ 4,940
Increase in specific prices (current cost) of property, plant and equipment held during the year (b)			$ 65,358
Reduction to net recoverable cost		$ (44,074)	(20,374)
Effect of increase in the general price level on property, plant and equipment			(87,308)
Excess of increase in the general price level over increase in specific prices of property, plant and equipment after reduction to net recoverable cost			(42,324)
Advantage resulting from the decrease in purchasing power of net monetary liabilities		35,752	35,752
Net		$ (8,322)	$ (6,572)

(a) Including the reduction to net recoverable cost, the income (loss) from continuing operations adjusted for general inflation would have been $(37,384,000).

(b) At December 31, 1979, property, plant and equipment, net of accumulated depreciation, all adjusted for changes in specific prices (current cost) was $741,128,000, while historical cost (net cost recoverable) was $445,347,000.

See Notes to Supplementary Financial Data on page 38.

PENNSYLVANIA POWER COMPANY
Five-Year Comparison of Selected Supplementary Financial Data
Adjusted for the Effects of Changing Prices For the Years Ended December 31, 1979

	1979	1978	1977	1976	1975
	Thousands of Dollars				
Operating Revenues					
As reported in the primary statements	$145,340	$119,118	$100,843	$ 89,583	$ 87,212
Adjusted to average 1979 dollars	$145,340	$132,529	$120,789	$114,225	$117,617
Historical Cost Information Adjusted for General Inflation					
(In Average 1979 Dollars)					
Income from continuing operations (excluding reduction to net recoverable cost)	$ 6,690				
Current Cost Information					
(In Average 1979 Dollars)					
Income from continuing operations (excluding reduction to net recoverable cost)	$ 4,940				
Excess of increase in the general price level over increase in specific prices of property, plant and equipment after reduction to net recoverable cost	$ (42,324)				
Other Information					
Common stockholder's equity at December 31 at net recoverable cost (Average 1979 Dollars)	$146,947				
Advantage resulting from the decrease in purchasing power of net monetary liabilities (Average 1979 Dollars)	$ 35,752				
Average consumer price index	217.4	195.4	181.5	170.5	161.2

Notes to the Supplementary Financial Data

The Consumer Price Index for All Urban Consumers (CPI-U) was used for converting historical amounts for property, plant and equipment into average 1979 dollars, thus giving an indication of the effect of general inflation on the principal assets of the Company.

Current cost of property, plant and equipment other than land was calculated by applying the Handy-Whitman Index of Public Utility Construction Costs for the North Central Division and the Bureau of Labor and Statistics engineering indices to functional accounts by vintage years, except for large construction projects which were trended based on the year that costs were incurred. The current cost of land was calculated by applying the CPI-U to the actual costs in the respective years of acquisition. The current cost data approximately reflects the current cost of acquiring property, plant and equipment identical to assets currently owned.

Depreciation expense adjusted for general inflation and for changing prices was determined using the same rates and methods used in calculating the provision in the primary financial statements. The accumulated provisions for depreciation were estimated for each functional class of property, plant and equipment by applying the Handy-Whitman Index to a vintaged theoretical reserve for depreciation.

Income taxes included in income from continuing operations adjusted for general inflation and for changing prices is the same as the provision reported in the primary financial statements, in conformity with SFAS No. 33.

During inflationary periods, the investment necessary to replace property, plant and equipment will be more than their original cost. Because the Company is permitted to recover in revenues, through a depreciation allowance, only the historical costs of such assets, the additional cost of plant as adjusted for changing prices is indicated as a "Reduction to net recoverable cost."

Net monetary liabilities of the Company consist primarily of long-term debt and preferred stock. During inflationary periods, the Company will be repaying these net monetary liabilities with dollars having less purchasing power than dollars had when the liability was originally incurred. The difference is indicated by the "Advantage resulting from the decrease in purchasing power of net monetary liabilities."

Directors and Officers

J. F. DUNLEVY
Vice President of the Company
New Castle, Pennsylvania

J. R. EDGERLY
Secretary and General Counsel of the Company, New Castle, Pennsylvania

D. BRUCE MANSFIELD
Retired—formerly Chairman of the Board and President of the Company
Akron, Ohio

V. A. OWOC
Executive Vice President of the Company's parent, Ohio Edison Company, Akron, Ohio

W. F. REEHER
Vice President of the Company
New Castle, Pennsylvania

JUSTIN T. ROGERS, JR.
Chairman of the Board of the Company, and President of its parent, Ohio Edison Company, Akron, Ohio

W. H. SAMMIS
Retired—formerly Chairman of the Board and President of the Company, Akron, Ohio

RAY E. SEMMLER
President of the Company
New Castle, Pennsylvania

C. M. WHITTAKER
Retired—formerly Chairman of the Board, Universal-Rundle Corporation, a plumbing fixture manufacturer, New Castle, Pennsylvania

M. L. WILSON
Treasurer of the Company
New Castle, Pennsylvania

G. L. WINGER
Group Vice President—Foundries, Midland-Ross Corporation, castings manufacturer, Sharon, Pennsylvania

JUSTIN T. ROGERS, JR.
Chairman of the Board

RAY E. SEMMLER
President

W. K. CONOVER
Vice President

J. F. DUNLEVY
Vice President

W. F. REEHER
Vice President

M. L. WILSON
Treasurer

J. R. EDGERLY
Secretary and General Counsel

R. P. ARMSTRONG
Assistant Secretary and Assistant Treasurer

W. A. MARGRAF
Assistant Secretary and Assistant Treasurer

ANGELINE COMPARONE
Assistant Secretary

DIVISION MANAGER
J. R. TOPPER
Mercer County

Mr. Rogers is president of the parent company, Ohio Edison Company. The principal employment of all other officers is with the Company.

REGISTRAR for Preferred Stock:
First Seneca Bank and Trust Company, Washington Centre,
New Castle, Pennsylvania 16101

TRANSFER AGENT
for Preferred Stock:
Office of the Company,
New Castle, Pennsylvania 16103

GENERAL OFFICES:
1 E. Washington Street,
New Castle, Pennsylvania 16103

Pennsylvania Power Company is an equal opportunity employer.

Pennsylvania Power Company
Annual Report
1 E. Washington Street
New Castle, PA 16103

U. S. Postage
Bulk Rate
PAID
Permit No. 158
New Castle, Pa.

MONEY
Kilowatt-hour sales, revenues rose. Costs also rose.
p. 5

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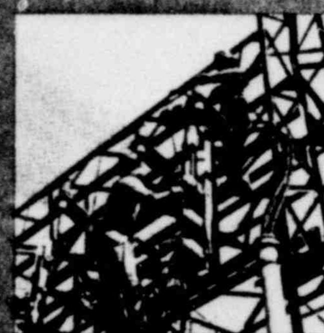

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SERVING CUSTOMERS
Four objectives guided our efforts.
p. 8

PROBLEMS PERSIST
Legal/environmental
p. 11

COMMUNICATIONS
Telling our story is an endless task.
p. 14