INTEGRYS ENERGY GROUP, INC.
Form 10-K
February 24, 2011

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-K

(Mark One)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2010

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ________________ to ___________________

| Commission File Number | Registrant; State of Incorporation; Address; and Telephone Number | IRS Employer Identification No. |
|---|---|---|
| 1-11337 | INTEGRYS ENERGY GROUP, INC.<br>(A Wisconsin Corporation)<br>130 East Randolph Street<br>Chicago, IL 60601<br>(312) 228-5400 | 39-1775292 |

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock, $1 par value | New York Stock Exchange |

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes [X] No [ ]

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes [ ] No [X]

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes [X ]   No [  ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.  See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

| | |
|---|---|
| Large accelerated filer [X] | Accelerated filer [  ] |
| Non-accelerated filer [  ] | Smaller reporting company [  ] |

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  [  ]   No  [X]

State the aggregate market value of the voting and
non-voting common equity held by non-affiliates of the Registrant.

$3,359,170,589 as of June 30, 2010

Number of shares outstanding of each class
of common stock, as of February 21, 2011

Common Stock, $1 par value, 78,007,885 shares

DOCUMENT INCORPORATED BY REFERENCE

Portions of the definitive proxy statement for the Integrys Energy Group, Inc. Annual Meeting of Shareholders to be held on May 11, 2011 are incorporated by reference into Part III.

INTEGRYS ENERGY GROUP, INC.

ANNUAL REPORT ON FORM 10-K
For the Year Ended December 31, 2010

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Acronyms Used in this Annual Report on Form 10-K

| | |
|---|---|
| AFUDC | Allowance for Funds Used During Construction |
| ASC | Accounting Standards Codification |
| ATC | American Transmission Company LLC |
| BACT | Best Available Control Technology |
| CAA | Clean Air Act |
| EEP | Enhanced Efficiency Program |
| EPA | United States Environmental Protection Agency |
| FASB | Financial Accounting Standards Board |
| FERC | Federal Energy Regulatory Commission |
| GAAP | United States Generally Accepted Accounting Principles |
| IBS | Integrys Business Support, LLC |
| ICC | Illinois Commerce Commission |
| ICR | Infrastructure Cost Recovery |
| IRS | United States Internal Revenue Service |
| ITC | Investment Tax Credit |
| LIFO | Last-in, First-out |
| MERC | Minnesota Energy Resources Corporation |
| MGU | Michigan Gas Utilities Corporation |
| MISO | Midwest Independent Transmission System Operator, Inc. |
| MPSC | Michigan Public Service Commission |
| MPUC | Minnesota Public Utility Commission |
| N/A | Not Applicable |
| NSG | North Shore Gas Company |
| OCI | Other Comprehensive Income |
| PEC | Peoples Energy Corporation |
| PEP | Peoples Energy Production Company |
| PGL | The Peoples Gas Light and Coke Company |
| PSCW | Public Service Commission of Wisconsin |
| SEC | United States Securities and Exchange Commission |
| SFAS | Statement of Financial Accounting Standards |
| UPPCO | Upper Peninsula Power Company |
| WDNR | Wisconsin Department of Natural Resources |
| WPS | Wisconsin Public Service Corporation |
| WRPC | Wisconsin River Power Company |

Forward-Looking Statements

In this report, Integrys Energy Group and its subsidiaries make statements concerning expectations, beliefs, plans, objectives, goals, strategies, and future events or performance. Such statements are "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements are subject to assumptions and uncertainties; therefore, actual results may differ materially from those expressed or implied by such forward-looking statements. Although Integrys Energy Group and its subsidiaries believe that these forward-looking statements and the underlying assumptions are reasonable, they cannot provide assurance that such statements will prove correct.

Forward-looking statements include, among other things, statements concerning management's expectations and projections regarding earnings, regulatory matters, fuel and natural gas costs, sources of electric energy supply, coal and natural gas deliveries, remediation costs, environmental expenditures, liquidity and capital resources, trends, estimates, completion of construction projects, and other matters.

Forward-looking statements involve a number of risks and uncertainties. Some risks that could cause results to differ from any forward-looking statement include those described in Item 1A of this Annual Report on Form 10-K for the year ended December 31, 2010. Other risks and uncertainties include, but are not limited to:

- Resolution of pending and future rate cases and negotiations (including the recovery of deferred costs) and other regulatory decisions impacting Integrys Energy Group's regulated businesses;
- The individual and cumulative impact of recent and future federal and state regulatory changes, including legislative and regulatory initiatives regarding deregulation and restructuring of the electric and natural gas utility industries; financial reform; health care reform; changes in environmental and other regulations, including but not limited to, greenhouse gas emissions, other environmental regulations impacting coal-fired generation facilities, energy efficiency mandates, renewable energy standards, and reliability standards; and changes in tax and other laws and regulations to which Integrys Energy Group and its subsidiaries are subject;
- Current and future litigation and regulatory proceedings, enforcement actions or inquiries, including but not limited to, manufactured gas plant site cleanup, third-party intervention in permitting and licensing projects, compliance with CAA requirements at generation plants, and prudence and reconciliation of costs recovered in revenues through automatic gas cost recovery mechanisms;
- The impacts of changing financial market conditions, credit ratings, and interest rates on the liquidity and financing efforts of Integrys Energy Group and its subsidiaries;
- The residual risks related to exiting parts of Integrys Energy Group's nonregulated energy services business, including settling certain provisions of the related sales agreements at costs greater than anticipated;
- The risks associated with changing commodity prices (particularly natural gas and electricity) and the available sources of fuel, natural gas, and purchased power, including their impact on margins, working capital, and liquidity requirements;
- Resolution of audits or other tax disputes with the IRS and various state, local, and Canadian revenue agencies;
- The effects, extent, and timing of additional competition or regulation in the markets in which Integrys Energy Group's subsidiaries operate;
- The retention of market-based rate authority;

The risk associated with the value of goodwill or other intangibles and their possible impairment;
Investment performance of employee benefit plan assets and the related impact on future funding requirements;
Changes in technology, particularly with respect to new, developing, or alternative sources of generation;
Effects of and changes in political and legal developments, as well as economic conditions and the related impact on customer demand, including the ability to attract and retain customers for the nonregulated energy services business and to adequately forecast energy usage for Integrys Energy Group's customers;

- Potential business strategies, including mergers, acquisitions, and construction or disposition of assets or businesses, which cannot be assured to be completed timely or within budgets;
- The direct or indirect effects of terrorist incidents, natural disasters, or responses to such events;
- The effectiveness of risk management strategies, the use of financial and derivative instruments, and the ability to recover costs from customers in rates associated with the use of those strategies and financial and derivative instruments;
- The risk of financial loss, including increases in bad debt expense, associated with the inability of Integrys Energy Group's and its subsidiaries' counterparties, affiliates, and customers to meet their obligations;
- Customer usage, weather, and other natural phenomena;
- The utilization of tax credit and loss carryforwards;
- Contributions to earnings by non-consolidated equity method and other investments, which may vary from projections;
- The effect of accounting pronouncements issued periodically by standard-setting bodies; and
- Other factors discussed elsewhere herein and in other reports filed by Integrys Energy Group from time to time with the SEC.

Except to the extent required by the federal securities laws, Integrys Energy Group and its subsidiaries undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

# PART I

## ITEM 1. BUSINESS

## A. GENERAL

References to "Notes" are to the Notes to the Consolidated Financial Statements included in this Annual Report on Form 10-K.

For additional information about Integrys Energy Group's business operations, including financial and geographic information about each reportable business segment, see Note 25, "Segments of Business," and Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Results of Operations."

### Integrys Energy Group, Inc.

Integrys Energy Group was incorporated in Wisconsin in 1993. Integrys Energy Group is a diversified energy holding company with regulated natural gas and electric utility operations, nonregulated energy operations, and an approximate 34% equity ownership interest in ATC.

### Natural Gas Utility Segment

The natural gas utility segment includes the regulated natural gas utility operations of WPS, MGU, MERC, PGL, and NSG. WPS, a Wisconsin corporation, began operations in 1883. MGU and MERC, both Delaware corporations, began operations upon the acquisition of existing natural gas distribution operations in Michigan and Minnesota, respectively, in April 2006 and July 2006, respectively. PGL and NSG, both Illinois corporations, began operations in 1855 and 1900, respectively. Integrys Energy Group acquired PGL and NSG in February 2007 in the PEC merger. For the last three years, all of the natural gas utility segment's revenues were earned, and all assets were located, within the United States.

### Electric Utility Segment

The electric utility segment includes the regulated electric utility operations of WPS and UPPCO. UPPCO, a Michigan corporation, began operations in 1884. For the last three years, all of the electric utility segment's revenues were earned, and all assets were located, within the United States.

### Integrys Energy Services

Integrys Energy Services, a Wisconsin corporation, was established in 1994. Integrys Energy Services is a diversified nonregulated retail energy supply and services company that primarily sells electricity and natural gas to commercial, industrial, and residential customers in deregulated markets. In addition, Integrys Energy Services invests in energy assets with renewable attributes.

### Electric Transmission Investment

The electric transmission investment segment consists of Integrys Energy Group's approximate 34% ownership interest in ATC. ATC is a federally regulated electric transmission company with operations in Wisconsin, Michigan, Minnesota, and Illinois. ATC began operations in 2001. See Note 8, "Investments in Affiliates, at Equity Method," for more information about ATC.

## Holding Company and Other Segment

The holding company and other segment includes the operations of the Integrys Energy Group holding company and the PEC holding company, along with any nonutility activities at WPS, MGU, MERC, UPPCO, PGL, NSG, and IBS. Equity earnings from Integrys Energy Group's investment in WRPC are included in the holding company and other segment.

## Available Information

Integrys Energy Group's annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements, registration statements, and any amendments to these documents are available, free of charge, on its website, www.integrysgroup.com, as soon as reasonably practicable after they are filed with or furnished to the SEC. Reports, statements, and amendments posted on Integrys Energy Group's website do not include access to exhibits and supplemental schedules electronically filed with the reports, statements, or amendments. Integrys Energy Group is not including the information contained on or available through its website as a part of, or incorporating such information by reference into, this Annual Report on Form 10-K.

You may obtain materials filed with the SEC by Integrys Energy Group at the SEC Public Reference Room at 100 F Street, NE, Washington, DC 20549. To obtain information on the operation of the Public Reference Room, you may call the SEC at 1-800-SEC-0330. You may also view Integrys Energy Group's reports, proxy statements, and other information (including exhibits) filed electronically with the SEC, at the SEC's website at www.sec.gov.

# B. REGULATED NATURAL GAS UTILITY OPERATIONS

Integrys Energy Group provides regulated natural gas utility service to approximately 1,673,000 residential, commercial and industrial, transportation, and other customers located in Chicago and northern suburbs of Chicago, northeastern Wisconsin and an adjacent portion of Michigan's Upper Peninsula, various cities and communities throughout Minnesota, and the southern portion of lower Michigan.

## Facilities

For information regarding the regulated natural gas facilities, see Item 2, "Properties." For Integrys Energy Group's utility plant asset book value, see Note 5, "Property, Plant, and Equipment."

## Natural Gas Supply

Integrys Energy Group's natural gas utilities manage portfolios of natural gas supply contracts, storage services, and pipeline transportation services designed to meet their varying customer usage patterns at the lowest reasonable cost.

Integrys Energy Group's regulated natural gas subsidiaries contract for fixed-term firm natural gas supplies with various natural gas suppliers each year (in the United States and Canada) to meet the demand of firm system sales customers. Integrys Energy Group's regulated natural gas supply requirements are met through a combination of fixed price purchases, index price purchases, storage (contracted and owned), peak-shaving facilities, and natural gas supply call options. To supplement natural gas supplies and minimize risk, Integrys Energy Group purchases additional natural gas supplies on the monthly and daily spot markets through fixed-term firm contracts.

Integrys Energy Group's natural gas utilities own two storage fields and contract with operators of underground storage fields for additional storage services. Integrys Energy Group's natural gas utilities contract with local distribution companies and interstate pipelines to purchase firm transportation services. Storage provides the ability to manage significant changes in daily natural gas demand and provides Integrys Energy Group with the ability to purchase steady levels of natural gas on a year-round basis, thus lowering supply cost volatility.  Integrys Energy Group's natural gas utilities utilize financial instruments such as commodity swaps and options as part of its hedging program to further reduce supply cost volatility during the winter period.  In addition, PGL utilizes its company-owned storage and pipeline assets as a natural gas hub.

For further information on Integrys Energy Group's regulated natural gas utility supply and transportation contracts, see Note 15, "Commitments and Contingencies."

Integrys Energy Group's natural gas utilities had adequate capacity to meet all firm natural gas demand obligations during 2010 and expect to have adequate capacity to meet all firm obligations during 2011.  Integrys Energy Group's natural gas utilities' forecast design peak-day throughput is 3,788 thousands of dekatherms (MDth) for the 2010 through 2011 heating season.

Deliveries to customers (including transportation customers) in MDth for Integrys Energy Group's regulated natural gas utility operations were as follows:

| (MDth) | 2010 | 2009 | 2008 |
|---|---|---|---|
| Natural gas purchases | 206,183 | 225,719 | 250,967 |
| Customer-owned natural gas received | 172,180 | 164,676 | 182,919 |
| Underground storage, net | 3,494 | 1,080 | (3,469) |
| Hub fuel in kind * | 176 | 141 | 135 |
| Liquefied petroleum gas | 4 | 12 | 5 |
| Owned storage cushion injection | (1,094) | (1,272) | (1,280) |
| Contracted pipeline and storage compressor fuel, franchise requirements, and unaccounted-for natural gas | (7,544) | (9,692) | (11,042) |
| Total | 373,399 | 380,664 | 418,235 |

* This delivered natural gas was originally provided by hub customers whose contract requires them to provide additional natural gas to compensate for unaccounted-for natural gas in future deliveries.

## Regulatory Matters

The natural gas retail rates of Integrys Energy Group's regulated natural gas utilities are regulated by the ICC, PSCW, MPSC, and MPUC.  These commissions have general supervisory and regulatory powers over public utilities in their respective jurisdictions.

Sales are made and services are rendered by the regulated natural gas utilities pursuant to rate schedules on file with the respective commissions containing various service classifications largely reflecting customers' different uses and levels of consumption.  In addition to the rates for distribution of natural gas, Integrys Energy Group's regulated natural gas utilities bill customers a natural gas charge representing third-party costs for purchasing, transporting, and storing natural gas, as well as gains, losses, and costs incurred under hedging programs, the amount of which is also subject to applicable commission authority.  Prudently incurred natural gas costs are passed directly through to customers in rates and, therefore, have no impact on margins.  Commissions in respective jurisdictions conduct annual proceedings regarding the reconciliation of revenues from the natural gas charge and related natural gas costs.

Most of the natural gas distributed by Integrys Energy Group is transported to its distribution systems by interstate pipelines.  The pipelines' services (transportation and storage) are regulated by the FERC under the Natural Gas Act and the Natural Gas Policy Act of 1978.  Under United States Department of Transportation regulations, the state commissions are responsible for monitoring the regulated natural gas utilities' safety compliance programs for their pipelines under 49 Code of Federal Regulations (CFR) Part 192 (Transportation of Natural and Other Gas by Pipeline: Minimum Federal Safety Standards) and 49 CFR Part 195 (Transportation of Hazardous Liquids by Pipeline).

PGL utilizes its company-owned storage and transmission assets as a natural gas hub, which consists of providing wholesale transportation and storage services in interstate commerce. This activity is regulated by the FERC. Revenues collected for use of the natural gas hub are credited to retail customers in rates.

All of Integrys Energy Group's natural gas utility subsidiaries are required to provide service and grant credit (with applicable deposit requirements) to customers within their service territories. The utilities are generally precluded from discontinuing service to residential customers who do not pay their bills during winter moratorium months. Federal government and certain state governments have legislation that provides for a limited amount of funding for assistance to low-income energy users, including customers of the utilities.

See Note 24, "Regulatory Environment," for more information regarding rate cases, decoupling mechanisms, and bad debt recovery mechanisms in place at the regulated natural gas utilities.

## Other Matters

### Seasonality

The natural gas throughput of Integrys Energy Group's regulated natural gas utilities generally follows a seasonal pattern because the heating requirements of customers are temperature driven. Specifically, customers typically use more natural gas during the winter months. During 2010, the regulated natural gas utility segment recorded approximately 69% of its revenues in January, February, March, November, and December.

### Competition

Although the natural gas retail rates of Integrys Energy Group's regulated natural gas utilities are regulated by various commissions, the utilities still face competition from other entities and forms of energy in varying degrees, particularly for large commercial and industrial customers who have the ability to switch between natural gas and alternate fuels. Due to the volatility of energy commodity prices, Integrys Energy Group has seen customers with dual fuel capability switch to alternate fuels for short periods of time, then switch back to natural gas as market rates change.

Natural gas transportation service and interruptible natural gas sales are offered to enable customers to better manage their energy costs. Transportation customers purchase natural gas directly from third-party natural gas suppliers and utilize Integrys Energy Group's natural gas utilities' distribution systems to transport the natural gas to their facilities. The natural gas utilities still earn a distribution charge for transporting the natural gas for these customers. The loss of revenue associated with the cost of natural gas now purchased from the third-party suppliers has no impact on the natural gas utilities' net income, as it is a pass-through cost to customers. Additionally, some customers have elected to purchase their natural gas directly from one of Integrys Energy Group's natural gas utility entities on an interruptible basis, as a means to reduce their costs. Customers continue to switch between firm system supply, interruptible system supply, and transportation service each year as the economics and service options change.

### Working Capital Requirements

The working capital needs of Integrys Energy Group's regulated natural gas utility operations vary significantly over time due to volatility in levels of natural gas inventories and the price of natural gas. Integrys Energy Group's regulated natural gas utilities' working capital needs are met by cash generated from operations and debt (both long-term and short-term). The seasonality of natural gas revenues causes the timing of cash collections to be concentrated from January through June. A portion of the winter natural gas supply needs is typically purchased and stored from April through November. Also, planned capital spending on the natural gas distribution facilities is concentrated in April through November. Because of these timing differences, the cash flow from customers is typically supplemented with temporary increases in short-term borrowings during the late summer and fall. Short-term debt is typically reduced over the January through June period.

## C. REGULATED ELECTRIC UTILITY OPERATIONS

Integrys Energy Group's regulated electric utility operations are provided through WPS and UPPCO to approximately 491,000 residential, commercial and industrial, wholesale, and other customers. WPS's regulated electric operations generate and distribute electricity mainly to northeastern Wisconsin and an adjacent portion of Michigan's Upper Peninsula. UPPCO provides electricity in Michigan's Upper Peninsula. Wholesale electric service is provided to various customers, including municipal utilities, electric cooperatives, energy marketers, other investor-owned utilities, and municipal joint action agencies.

In 2010, WPS reached a firm net design peak of 2,292 megawatts (MW) on August 12. At the time of this summer peak, WPS's total firm resources (i.e., generation plus firm purchases) totaled 2,945 MW. As a result of continually reaching demand peaks in the summer months, primarily due to air conditioning demand, the summer period is the most relevant for WPS's regulated electric utility capacity. The PSCW requires WPS to maintain a planning reserve margin above its projected annual peak demand forecast to help ensure reliability of electric service to its customers. WPS and UPPCO expect future supply reserves to meet the minimum planning reserve margin criteria in 2011. The PSCW established a 14.5% reserve margin requirement for long-term planning (planning years two through ten), and the short-term (planning year one) reserve margin for Wisconsin utilities follows the planning reserve margin established by MISO under Module E of its Open Access Transmission and Energy Markets Tariff. In 2010, UPPCO reached a firm net design peak of 129 MW on August 30. At the time of this peak, UPPCO's total firm resources totaled 133 MW. The MPSC has not established minimum guidelines for future supply reserves; however, the MISO planning reserve margin requirements also apply to UPPCO.

WPS and UPPCO had adequate capacity through company-owned generation units and power purchase contracts to meet all firm electric demand obligations during 2010 and expect to have adequate capacity to meet all obligations during 2011.

### Facilities

For a complete listing of Integrys Energy Group's regulated electric utility facilities, see Item 2, "Properties." For Integrys Energy Group's utility plant asset book value, see Note 5, "Property, Plant, and Equipment."

### Electric Supply

Both WPS and UPPCO are members of MISO, a FERC-approved, independent, non-profit organization, which operates a financial and physical electric wholesale market in the Midwest. WPS and UPPCO offer their generation and bid their customer load into the MISO market. MISO evaluates WPS's, UPPCO's, and other market participants' energy injections into, and withdrawals from, the system to economically dispatch electricity within the system. MISO settles the participants' offers and bids based on locational marginal prices, which are market-driven values based on the specific time and location of the purchase and/or sale of energy.

Electric Generation and Supply Mix

The sources of Integrys Energy Group's regulated electric utility supply were as follows:

| (Millions)<br>Energy Source (kilowatt-hours) | 2010 | 2009 | 2008 |
|---|---|---|---|
| Company-owned generation units | | | |
| Coal | 10,232.9 | 8,974.3 | 9,570.9 |
| Hydroelectric | 306.5 | 225.9 | 261.2 |
| Wind | 287.7 | 46.4 | 17.8 |
| Natural gas, fuel oil, and tire derived | 105.4 | 71.4 | 201.7 |
| Total company-owned generation units | 10,932.5 | 9,318.0 | 10,051.6 |
| Power purchase contracts | | | |
| Nuclear (Kewaunee Power Station) | 2,940.8 | 2,663.9 | 2,656.8 |
| Natural gas (Fox Energy Center, LLC and Combined Locks Energy Center, LLC) | 608.4 | 673.7 | 699.5 |
| Hydroelectric | 526.7 | 569.5 | 369.4 |
| Wind | 149.1 | 136.9 | 109.0 |
| Other | 205.5 | 571.1 | 167.8 |
| Total power purchase contracts | 4,430.5 | 4,615.1 | 4,002.5 |
| Purchased power from MISO | 781.9 | 1,898.9 | 1,934.0 |
| Purchased power from other | 342.9 | 54.4 | 78.9 |
| Total purchased power | 5,555.3 | 6,568.4 | 6,015.4 |
| Opportunity sales | | | |
| Sales to MISO | (734.5) | (462.5) | (539.8) |
| Net sales to other | (248.4) | (450.5) | (303.2) |
| Total opportunity sales | (982.9) | (913.0) | (843.0) |
| Total Integrys Energy Group electric utility supply | 15,504.9 | 14,973.4 | 15,224.0 |

Fuel Costs

The cost of fuel per generation of one million British thermal units (Btus) was as follows:

| Fuel Type | 2010 | 2009 | 2008 |
|---|---|---|---|
| Coal | $2.05 | $1.94 | $1.78 |
| Natural gas | 6.28 | 6.73 | 9.74 |
| Fuel oil | 18.44 | 17.09 | 19.07 |

Coal Supply

Coal is the primary fuel source for WPS's regulated electric generation facilities. WPS's regulated fuel portfolio strategy is to maintain a 35- to 45-day supply of coal at each plant site. The majority of the coal is purchased from Powder River Basin mines located in Wyoming. This low sulfur coal has been WPS's lowest cost coal source from any of the subbituminous coal-producing regions in the United States. Historically, WPS has purchased coal directly from the producer for its wholly owned plants. WPS purchases the coal for Weston 4, and Dairyland Power Cooperative reimburses WPS for its share of the coal costs. Wisconsin Power and Light purchases coal for the jointly owned Edgewater and Columbia plants and is reimbursed by WPS for its share of the coal costs. At December 31, 2010, WPS had coal transportation contracts in place for 90% of its 2011 coal transportation requirements. For more information on coal purchases and coal deliveries under contract, see Note 15, "Commitments and Contingencies."

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Power Purchase Agreements

Integrys Energy Group's regulated electric utilities enter into short-term and long-term power purchase agreements to meet a portion of their electric energy supply needs. The most significant of these is an agreement through 2013 with Dominion Energy Kewaunee, LLC to purchase energy and capacity from the Kewaunee Power Station consistent with volumes available when WPS owned the facility. For more information on power purchase obligations, see Note 15, "Commitments and Contingencies."

## Regulatory Matters

Integrys Energy Group's electric utility operations are regulated by the PSCW, MPSC, and FERC. WPS's retail electric rates are regulated by the PSCW and MPSC, and UPPCO's retail electric rates are regulated by the MPSC. The FERC regulates wholesale electric rates for WPS and UPPCO. In 2010, retail electric revenues accounted for 80.6% of total electric revenues, while wholesale electric revenues accounted for 19.4% of total electric revenues.

The PSCW sets rates through its ratemaking process, which is based upon recovery of operating costs and a return on invested capital. One of the cost recovery components is fuel and purchased power, which is governed by a fuel window mechanism, as described in Note 1(f), "Summary of Significant Accounting Policies – Revenue and Customer Receivables." The MPSC and FERC ratemaking processes are similar to those of the PSCW, with the exception of fuel and purchased power, which are recovered on a one-for-one basis.

See Note 24, "Regulatory Environment," for information regarding rate cases and decoupling mechanisms of Integrys Energy Group's electric utilities.

Hydroelectric Licenses

WPS, UPPCO, and WRPC (a company in which WPS has 50% ownership) have long-term licenses from the FERC for all of their hydroelectric facilities.

## Other Matters

Seasonality

Integrys Energy Group's regulated electric utility sales in Wisconsin generally follow a seasonal pattern due to the air conditioning requirements of customers, which are primarily impacted by the variability of summer temperatures. Integrys Energy Group's regulated electric utility sales in Michigan do not follow a significant seasonal trend due to cooler climate conditions in the Upper Peninsula of Michigan.

Competition

The retail electric utility market in Wisconsin is regulated by the PSCW. Retail electric customers currently do not have the ability to choose their electric supplier. However, in order to increase sales, utilities work to attract new commercial and industrial customers into their service territories. As a result, there is competition among utilities to keep energy rates low. Wisconsin utilities have continued to refine regulated tariffs in order to pass on the true cost of electricity to each class of customer by reducing or eliminating rate subsidies among different ratepayer classes. Although Wisconsin electric energy markets are regulated, utilities still face competition from other energy sources, such as self-generation by large industrial customers and alternative energy sources.

Michigan electric energy markets are open to competition; however, an active competitive market has not yet developed in the Upper Peninsula of Michigan, primarily due to a lack of excess generation and transmission system capacity.

## D. INTEGRYS ENERGY SERVICES

Integrys Energy Services and its subsidiaries market electricity, natural gas and related products in various retail markets, serving commercial and industrial customers, as well as direct and "aggregated" small commercial and residential customers. Aggregated customers are municipalities, associations, or groups of customers that have joined together to negotiate purchases of electric or natural gas energy as a larger group.

Integrys Energy Services is investing in and promoting renewable energy, which it believes is important to the future of the energy industry. Clean, renewable, and efficient energy sources are developed, acquired, owned, and operated by Integrys Energy Services. Integrys Energy Services assists customers with selecting an energy solution that meets their needs and collaborates with developers of wholesale energy projects to overcome challenges with integrating the technical, regulatory, and financial aspects of their projects.

Integrys Energy Services utilizes physical and financial derivative instruments, including forwards, futures, options, and swaps, to manage its exposure to market risks from its energy assets and energy supply portfolios in accordance with limits and approvals established in its risk management and credit policies.

### Recent Developments

Throughout 2009 and 2010, Integrys Energy Services was repositioned to focus on serving retail natural gas and retail electric customers concentrated in the northeast quadrant of the United States, and investing in energy assets with renewable attributes. See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Introduction," and Note 4, "Dispositions," for a discussion of the current strategy for Integrys Energy Services.

In October 2010, Integrys Energy Services announced the launch of a joint venture with Duke Energy Generation Services to build and finance distributed solar projects throughout the United States. Duke Energy Generation Services and Integrys Energy Services will equally supply the necessary equity capital for construction and ownership of these projects. Over the next two years, the companies intend to invest up to $180 million, in the aggregate, of total project capital. See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Future Capital Requirements and Resources," for estimated construction expenditures for Integrys Energy Services.

### Energy Supply

Physical supply obligations are created when Integrys Energy Services executes forward retail customer sales contracts. Integrys Energy Services' electricity supply requirements are primarily met through the procurement of electricity in the wholesale market. Integrys Energy Services does not own any natural gas reserves, so all natural gas supply is procured from producers and other suppliers in the wholesale market.

#### Retail Electric

The majority of Integrys Energy Services' obligations to provide physical electricity result from forward retail sales to commercial and industrial customers, many of which are through full-requirements contracts. Integrys Energy Services uses bilateral electricity purchase agreements from generation companies and other marketers, as well as regional power pools to meet those obligations.

Retail Natural Gas

The majority of Integrys Energy Services' obligations to provide physical natural gas result from forward retail sales to commercial and industrial customers, as well as some residential customers.  Natural gas is sourced in the wholesale market at the customer demand regions, or in some cases from supply regions and is transported to the customer demand regions under natural gas transportation contracts.

## Facilities

For information regarding the energy asset facilities owned by Integrys Energy Services, see Item 2, "Properties."  For Integrys Energy Group's nonregulated plant asset book value, see Note 5, "Property, Plant, and Equipment."

## Fuel Supply for Generation Facilities

Integrys Energy Services' fuel inventory policy varies for each generation facility depending on the type of fuel used.  The natural gas-fired facilities (82.0% of its installed generation portfolio) are subject to market price volatility, and are dispatched to produce energy only when it is economical to do so.  The Westwood facility, located in Pennsylvania (12.5% of its installed generation portfolio), is Integrys Energy Services' only coal-fired merchant generation facility.  The Westwood facility burns waste coal left behind by mining operations and has several years' supply on site.  All fuel is located within a seven-mile radius of the facility.  The renewable energy facilities (5.5% of its installed generation portfolio) are all powered by renewable resources such as solar irradiance or landfill gas.  There is no market price risk associated with the fuel supply of these facilities; however, production at these facilities can be intermittent due to the availability of the renewable energy resource.

## Regulatory Matters

Integrys Energy Services is a FERC-authorized power marketer and has all of the licenses required to conduct business in the states in which it operates.

## Other Matters

Customer Segmentation

As of December 31, 2010, Integrys Energy Services was delivering electricity and natural gas to retail customers in the northeast quadrant of the United States.  Integrys Energy Services periodically reviews and evaluates the profitability of its operations in each of its markets.  Integrys Energy Services continues to concentrate on adding customers in existing markets and emphasizing business that provides the appropriate rate of return, but currently has no plans to expand into new geographic regions.  See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Introduction," for a discussion of the current strategy for Integrys Energy Services.

As of December 31, 2010, Integrys Energy Services' largest electric markets included the Illinois, New York, Mid-Atlantic, and New England regions.  Integrys Energy Services' largest natural gas markets included Wisconsin, Illinois, Michigan, and Ohio.

Although Integrys Energy Services is not dependent on any one customer segment, a significant percentage of its retail sales volume is derived from industries related to paper and allied products, general government and national security, food and kindred products, schools (including primary, secondary, colleges, and universities), chemicals and paint, and steel and foundries.

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Seasonality

Integrys Energy Services believes that its business, in the aggregate, is not seasonal, even though certain products sell more heavily in certain seasons than in others. Sales of natural gas generally peak in the winter months, while sales of electricity generally peak in the summer months. Integrys Energy Services' business can be volatile as a result of market conditions and the related market opportunities available to its customers.

Competition

Integrys Energy Services is a nonregulated retail energy marketer that competes against regulated utilities and other retail energy marketers. Integrys Energy Services competes with other energy providers on the basis of price, reliability, customer service, product offerings, financial strength, consumer convenience, performance, and reputation.

The competitive landscape differs in each regional area and within each targeted customer segment. For residential and small commercial customers, the primary competitive challenges come from the incumbent utility and affiliated utility marketing companies. The large commercial, institutional, and industrial segments are very competitive in most markets with nearly all natural gas customers having already switched away from utilities to an alternative energy provider. National affiliated marketers, energy producers, and other independent retail energy companies compete for customers in this segment.

The incumbent regulated utilities and the nationally-branded utility affiliates typically benefit from the economies of scale derived from the strength of substantial asset-based balance sheets and vertically integrated business models that combine production, transmission, and distribution assets. These advantages are offset by the lack of flexibility to offer multiple product choices to their customers.

The local utilities have the advantage of long-standing relationships with their customers, and they have longer operating histories, greater financial and other resources, and greater name recognition in their markets than Integrys Energy Services. In addition, local utilities have been subject to many years of regulatory oversight and, thus, have a significant amount of experience regarding the policy preferences of their regulators. Local utilities may seek to decrease their tariff retail rates to limit or preclude opportunities for competitive energy suppliers and may seek to establish rates, terms, and conditions to the disadvantage of competitive energy suppliers.

Working Capital

The working capital needs of Integrys Energy Services vary significantly over time due to volatility in commodity prices and related margin calls, and levels of natural gas storage inventories. Integrys Energy Services' working capital needs are met by cash generated from operations, equity infusions, and debt (both long-term and short-term). As of December 31, 2010, Integrys Energy Services had the ability to borrow up to $765.0 million through an intercompany credit facility with Integrys Energy Group. As of December 31, 2010, Integrys Energy Group had provided total parental guarantees of $566.6 million on behalf of Integrys Energy Services, which includes guarantees for the retained retail business as well as residual guarantees related to assets sold.

## E. ENVIRONMENTAL MATTERS

For information on environmental matters related to Integrys Energy Group and its subsidiaries, see Note 15, "Commitments and Contingencies."

## F. CAPITAL REQUIREMENTS

For information on Integrys Energy Group's capital requirements, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources."

## G. EMPLOYEES

At December 31, 2010, Integrys Energy Group's consolidated subsidiaries had the following employees:

| | Total Number of Employees | Percentage of Employees Covered by Collective Bargaining Agreements |
|---|---|---|
| WPS | 1,363 | 65% |
| IBS | 1,206 | - |
| PGL | 1,082 | 83% |
| Integrys Energy Services | 289 | - |
| MERC | 216 | 19% |
| NSG | 166 | 81% |
| MGU | 159 | 69% |
| UPPCO | 131 | 82% |
| Total | 4,612 | 47% |

Integrys Energy Group's subsidiaries have collective bargaining agreements with various unions which are summarized in the table below.

| Union | Subsidiary | Contract Expiration Date |
|---|---|---|
| Local 310 of the International Union of Operating Engineers | WPS | October 13, 2012 |
| Local 18007 of the Utility Workers Union of America | PGL | April 30, 2013 |
| Local 31 of the International Brotherhood of Electrical Workers, AFL CIO | MERC | May 31, 2011 |
| Local 2285 of the International Brotherhood of Electrical Workers | NSG | June 30, 2013 |
| Local 12295 of the United Steelworkers of America, AFL CIO CLC | MGU | January 15, 2015 |
| Local 417 of the Utility Workers Union of America, AFL CIO | MGU | February 15, 2012 |
| Local 510 of the International Brotherhood of Electrical Workers, AFL CIO | UPPCO | April 12, 2014 |

H. EXECUTIVE OFFICERS OF INTEGRYS ENERGY GROUP

| Name and Age (1) | | Position and Business Experience During Past Five Years | Effective Date |
|---|---|---|---|
| Charles A. Schrock | 57 | Chairman, President and Chief Executive Officer | 04-01-10 |
| | | President and Chief Executive Officer | 01-01-09 |
| | | President and Chief Executive Officer of WPS | 05-31-08 |
| | | President of WPS | 02-21-07 |
| | | President and Chief Operating Officer – Generation – WPS | 08-15-04 |
| Lawrence T. Borgard | 49 | President and Chief Operating Officer – Utilities | 04-05-09 |
| | | President and Chief Operating Officer – Integrys Gas Group (2) | 02-21-07 |
| | | President and Chief Operating Officer – Energy Delivery – WPS | 08-15-04 |
| Phillip M. Mikulsky | 62 | Executive Vice President – Business Performance and Shared Services | 12-26-10 |
| | | Executive Vice President – Corporate Development and Shared Services | 09-21-08 |
| | | Executive Vice President and Chief Development Officer | 02-21-07 |
| | | Executive Vice President – Development | 09-12-04 |
| Mark A. Radtke | 49 | Executive Vice President and Chief Strategy Officer | 12-26-10 |
| | | Chief Executive Officer – Integrys Energy Services | 01-10-10 |
| | | President and Chief Executive Officer – Integrys Energy Services | 06-01-08 |
| | | President – Integrys Energy Services (previously named WPS Energy Services, Inc.) | 10-17-99 |
| Joseph P. O'Leary | 56 | Senior Vice President and Chief Financial Officer | 06-04-01 |
| Diane L. Ford | 57 | Vice President and Corporate Controller | 02-21-07 |
| | | Vice President – Controller and Chief Accounting Officer | 07-11-99 |
| William J. Guc | 41 | Vice President and Treasurer | 12-01-10 |
| | | Vice President – Finance and Accounting and Controller – Integrys Energy Services | 03-07-10 |
| | | Vice President and Controller – Integrys Energy Services | 09-21-08 |
| | | Controller – Integrys Energy Services (previously named WPS Energy Services) | 02-21-05 |
| William D. Laakso | 48 | Vice President – Human Resources | 09-21-08 |

| | | | |
|---|---|---|---|
| | | Interim Vice President – Human Resources – IBS | 05-15-08 |
| | | Director – Workforce Planning and Organizational Design – WPS | 08-12-07 |
| | | Director of Organizational Development – WPS | 12-12-05 |
| | | | |
| James F. Schott | 53 | Vice President – External Affairs | 03-22-10 |
| | | Vice President – Regulatory Affairs | 07-18-04 |
| | | | |
| Barth J. Wolf | 53 | Vice President, Chief Legal Officer and Secretary | 07-31-07 |
| | | Vice President – Legal Services and Chief Compliance Officer – IBS | 02-21-07 |
| | | Secretary and Manager – Legal Services | 09-19-99 |
| | | | |
| Daniel J. Verbanac | 47 | President – Integrys Energy Services | 01-01-10 |
| | | Chief Operating Officer – Integrys Energy Services (previously named WPS Energy Services) | 02-15-04 |

(1) All ages are as of January 1, 2011. None of the executives listed above are related by blood, marriage, or adoption to any of the other officers listed or to any director of Integrys Energy Group. Each officer holds office until his or her successor has been duly elected and qualified, or until his or her death, resignation, disqualification, or removal.

(2) The Integrys Gas Group includes PGL, NSG, MERC, and MGU.

ITEM 1A. RISK FACTORS

You should carefully consider the following risk factors, as well as the other information included or incorporated by reference in this Annual Report on Form 10-K, when making an investment decision.

Integrys Energy Group is subject to changes in government regulation, which may have a negative impact on its businesses, financial position, and results of operations.

Integrys Energy Group is subject to comprehensive regulation by several federal and state regulatory agencies and local governmental bodies, which significantly influences its operating environment and may affect Integrys Energy Group's ability to recover costs from customers of its regulated operations. Many aspects of Integrys Energy Group's operations are regulated, including, but not limited to, construction and operation of facilities, conditions of service, the issuance of securities, and the rates that it can charge customers. Integrys Energy Group is required to have numerous permits, approvals, and certificates from these agencies to operate its business. Failure to comply with any applicable rules or regulations may lead to penalties or customer refunds, which could have a material impact on the financial results of Integrys Energy Group.

Existing statutes and regulations may be revised or reinterpreted by these agencies, or these agencies may adopt new laws and regulations that apply to Integrys Energy Group. Integrys Energy Group is unable to predict the impact on its businesses and operating results of any such actions by these agencies. However, changes in regulations or the imposition of additional regulations may require Integrys Energy Group to incur additional expenses or change business operations, which may have an adverse impact on results of operations.

The rates that Integrys Energy Group's regulated utilities are allowed to charge for their retail and wholesale services are the most important factors influencing its business, financial position, results of operations, and liquidity. While rate regulation is premised on providing an opportunity to earn a reasonable rate of return on invested capital, there is no assurance that the applicable regulatory commissions will judge all the costs of the regulated utilities to have been prudently incurred or that the regulatory process will always result in rates that will produce full recovery of such costs or provide for a reasonable return on equity. Certain items that would otherwise be immediately recognized as revenues and expenses are deferred as regulatory assets and regulatory liabilities for future recovery or refund to customers, as authorized by regulators. Future recovery of regulatory assets is not assured, and is generally subject to review by regulators in rate proceedings for matters such as prudence and reasonableness. If recovery of costs is not approved or is no longer deemed probable, regulatory assets would be recognized in current period expense and could have a material impact on Integrys Energy Group's financial results.

Costs of environmental compliance, liabilities, fines, penalties, and litigation could exceed Integrys Energy Group's estimates.

Compliance with current and future federal and state environmental laws and regulations may result in increased capital, operating, and other costs, including remediation and containment expenses and monitoring obligations. Integrys Energy Group cannot predict with certainty the amount and timing of all future expenditures (including the potential or magnitude of fines or penalties) related to environmental matters because of the difficulty of estimating cleanup and compliance costs and the possibility that changes will be made to the current environmental laws and regulations.

Integrys Energy Group's natural gas utility subsidiaries are accruing liabilities and deferring costs (recorded as regulatory assets) incurred in connection with their former manufactured gas plant sites, including related legal expenses, pending recovery through rates or from other entities. Regulatory assets reflect the net amount of (1) costs incurred to date, (2) carrying costs incurred to date (excluding those for WPS, which are not recoverable), (3) amounts recovered from insurance companies, other entities and customers, and (4) management's best estimates of the costs Integrys Energy Group will incur in the future for investigating and remediating the former manufactured gas plant sites. Integrys

Energy Group believes that any of these costs that are not recoverable from other entities or from insurance carriers are recoverable through rates for utility services under approved mechanisms for the recovery of prudently incurred costs. A change in these rate recovery mechanisms, however, or a decision by the applicable state commission that some or all of these costs were not prudently incurred, could result in the present recognition as expense of some or all of these costs. For more information, see Note 15, "Commitments and Contingencies."

WPS owns coal-fired electric generating facilities at which it has performed maintenance activities that the EPA alleges were subject to CAA New Source Review permitting requirements. Depending on potential settlement terms or a court decision, WPS could be required to install environmental controls, change operations, shut down certain plants, undertake supplemental environmental projects, and/or pay fines.

In addition, impacts resulting from future federal or state regulation regarding mercury, sulfur dioxide, and nitrogen oxide emissions, as well as the management of coal combustion byproducts, are uncertain. The cumulative effect of any such regulations could potentially lead to certain coal-fired electric generating facilities being uneconomical to run. There is also uncertainty in quantifying liabilities under environmental laws that impose joint and several liability on all potentially responsible parties.

Citizen groups that feel environmental regulations are not being sufficiently enforced by environmental regulatory agencies may also bring citizen enforcement actions against Integrys Energy Group. Such actions could seek penalties, injunctive relief, and costs of litigation. Private citizens can also bring lawsuits to recover environmental damages they believe they have incurred.

Integrys Energy Group may face significant costs to comply with the regulation of greenhouse gas emissions.

Political interest in climate change and the effects of greenhouse gas emissions, most notably carbon dioxide, are a concern for the energy industry. Although no legislation is currently pending that would affect Integrys Energy Group, state or federal legislation could be passed in the future to regulate greenhouse gases. In addition, the EPA has adopted regulations under the CAA that apply to permitting new or significantly modified facilities. The EPA also announced its intent to develop new source performance standards for greenhouse gas emissions for new and modified, as well as existing, electric utility steam generating units. Until legislation is passed at the federal or state level or the EPA adopts final rules for electric utility steam generating units, it remains unclear as to (1) which industry sectors will be impacted, (2) when compliance will be required, (3) the magnitude of the greenhouse gas emissions reductions that will be required, and (4) the costs and opportunities associated with compliance. Integrys Energy Group is evaluating both the technical and cost implications that may result from future state, regional, or federal greenhouse gas regulatory programs, but at this time, it is uncertain as to the effect climate change regulation may have on Integrys Energy Group's future operations, capital expenditures, and financial results.

It is possible that future carbon regulation will increase the cost of electricity produced at coal-fired generation units and may affect the capital expenditures Integrys Energy Group would make at its generation units. At this time, there is no commercially available technology for removing carbon dioxide from a pulverized coal-fired plant. In addition, future legislation designed to reduce greenhouse gas emissions could make some generating units uneconomical to maintain or operate and could impact future results of operations, cash flows, and financial condition if such costs are not recoverable through regulated rates.

Integrys Energy Group's natural gas delivery systems may generate fugitive gas as a result of normal operations and as a result of excavation, construction, and repair of natural gas delivery systems. Fugitive gas typically vents to the atmosphere and consists primarily of methane, a greenhouse gas. Carbon dioxide is also a byproduct of natural gas consumption. As a result, future legislation to regulate the emission of greenhouse gases could increase the price of natural gas, restrict the use of natural gas, adversely affect the ability to operate our natural gas facilities, and/or reduce natural gas demand, which

could have a material adverse impact on Integrys Energy Group’s results of operations and financial condition.

Integrys Energy Group's operations are subject to risks beyond its control, including but not limited to customer usage, weather, terrorist attacks, or acts of war.

Integrys Energy Group's revenues are affected by the demand for electricity and natural gas. That demand can vary greatly based upon:

- Fluctuations in economic activity and growth in Integrys Energy Group's regulated service areas, as well as areas in which its nonregulated subsidiaries operate;
- Weather conditions, seasonality, and temperature extremes; and
- The amount of additional energy available from current or new competitors.

General economic conditions and customers focusing on energy efficiency in Integrys Energy Group's service areas may result in a decrease in demand for electricity or natural gas, which could have an adverse impact on Integrys Energy Group's results of operations, financial condition, and cash flows.

Weather conditions directly influence the demand for electricity and natural gas and affect the price of energy commodities.

In addition, the cost of repairing damage to Integrys Energy Group's facilities due to storms, natural disasters, wars, terrorist acts, and other catastrophic events, in excess of insurance limits established for such repairs or excluded by insurance policies, may adversely impact Integrys Energy Group's results of operations, financial condition, and cash flows. The occurrence or risk of occurrence of future terrorist activity and the high cost or potential unavailability of insurance to cover such terrorist activity may impact Integrys Energy Group's results of operations and financial condition in unpredictable ways. These actions could also result in disruptions of electricity and fuel markets.

Adverse capital and credit market conditions could negatively affect Integrys Energy Group's ability to meet liquidity needs, access capital, and/or grow or sustain its current business. Cost of capital and disruptions, uncertainty, and/or volatility in the financial markets could adversely impact the results of operations and financial condition of Integrys Energy Group, as well as exert downward pressure on its stock price.

Having access to the credit and capital markets, at a reasonable cost, is necessary for Integrys Energy Group to fund its operations and capital requirements. The capital and credit markets provide Integrys Energy Group with liquidity to operate and grow its businesses that is not otherwise provided from operating cash flows and also support the ability of Integrys Energy Group to provide credit support for the nonregulated operations of Integrys Energy Services. Disruptions, uncertainty, and/or volatility in those markets could increase Integrys Energy Group's cost of capital or limit the availability of capital. If Integrys Energy Group or its subsidiaries are unable to access the credit and capital markets on terms that are reasonable, they may have to delay raising capital, issue shorter-term securities, and/or bear an increased cost of capital. This, in turn, could impact Integrys Energy Group's ability to grow or sustain its current businesses, cause a reduction in earnings, result in a credit rating downgrade, and/or limit Integrys Energy Group's ability to sustain its current common stock dividend level.

A reduction in Integrys Energy Group's or its subsidiaries' credit ratings could materially and adversely affect its business, financial position, results of operations, and liquidity.

Integrys Energy Group cannot be sure that any of Integrys Energy Group's or its subsidiaries' credit ratings will remain in effect for any given period of time or that a credit rating will not be lowered by a rating agency if, in the rating agency’s judgment, circumstances in the future so warrant.  Any downgrade could:

- Require the payment of higher interest rates in future financings and possibly reduce the potential pool of creditors;
- Increase borrowing costs under certain existing credit facilities;
- Limit access to the commercial paper market;
- Limit the availability of adequate credit support for Integrys Energy Services' operations; and
- Require provision of additional credit assurance, including cash margin calls, to contract counterparties.

Fluctuating commodity prices may reduce energy margins and result in liquidity constraints.

The margins and liquidity requirements of Integrys Energy Group’s regulated and nonregulated businesses are impacted by changes in the forward and current market prices of natural gas, coal, electricity, renewable energy credits, and ancillary services.  Changes in price could result in:

- Higher working capital costs, particularly related to natural gas inventory, accounts receivable, and cash collateral postings;
- Increased liquidity requirements due to potential counterparty margin calls related to the use of derivative instruments to manage commodity price and volume exposure;
- Reduced profitability to the extent that reduced margins, increased bad debt, and interest expenses are not recovered through rates;
- Higher rates charged to regulated customers, which could impact the company’s competitive position;
- Reduced demand for energy, which could impact margins and operating expenses; and
- Shutting down of generation facilities if the cost of generation exceeds the market price for electricity.

Counterparties and customers may not meet their obligations.

Integrys Energy Group is exposed to the risk that counterparties to various arrangements who owe Integrys Energy Group money, electricity, natural gas, coal, or other commodities or services will not be able to perform their obligations.  Should the counterparties to these arrangements fail to perform, Integrys Energy Group might be forced to replace or to sell the underlying commitment at then-current market prices.  In such event, Integrys Energy Group might incur losses, or its results of operations, financial position, or liquidity could otherwise be adversely affected.

Some of Integrys Energy Group's customers are experiencing, or may experience, financial problems that could have a significant impact on their creditworthiness.  Integrys Energy Group cannot provide assurance that its financially distressed customers will not default on their obligations to Integrys Energy Group and that such a default will not have a material adverse impact on Integrys Energy Group's business, financial position, results of operations, or cash flows.  Furthermore, the bankruptcy of one or more of its customers, or some other similar proceeding or liquidity constraint, could adversely impact Integrys Energy Group's receivable collections and additional allowances may be required, which could adversely affect its operating results.  In addition, such events might force customers to reduce or curtail their future use of Integrys Energy Group's products and services, which could have a material adverse impact on Integrys Energy Group’s results of operations and financial condition.

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Any change in Integrys Energy Group's ability to sell electricity generated from its facilities at market-based rates may impact earnings.

The FERC has authorized certain of Integrys Energy Group's subsidiaries to sell generation from certain of its facilities at market prices. The FERC retains the authority to modify or withdraw this market-based rate authority. If the FERC determines that the market is not workably competitive, that Integrys Energy Group or its subsidiaries possess market power, that they are not charging just and reasonable rates, or that they have not complied with the rules required in order to have market-based rates, the FERC may require Integrys Energy Group's subsidiaries to sell power at a price based upon the costs incurred in producing the power. Integrys Energy Group's revenues and profit margins may be negatively affected by any reduction by the FERC of the rates it may receive.

Integrys Energy Group may not be able to utilize tax credit and/or net operating loss carryforwards.

Integrys Energy Group has significantly reduced its consolidated federal and state income tax liability in the past through tax credits and tax net operating loss carryforwards available under the applicable tax codes. Integrys Energy Group has not fully utilized these tax credits and tax net operating loss carryforwards in its previous tax filings, but expects to prior to their expiration in future filings. However, Integrys Energy Group may not be able to fully utilize the tax credits and tax net operating losses available as carryforwards if its future federal and state taxable income and related income tax liability is insufficient to permit the use of such credits and losses.

In addition, any future disallowance of some or all of those tax credits or tax net operating loss carryforwards as a result of legislative change or adverse determination by one of the applicable taxing jurisdictions could materially affect Integrys Energy Group's tax obligations.

Integrys Energy Group has recorded goodwill and other intangibles that could become impaired and adversely affect financial results.

To the extent the value of goodwill or other intangibles becomes impaired, Integrys Energy Group has had to, and in the future, may also be required to, incur material noncash charges relating to such impairments. Such impairment charges could have a material impact on the financial results of Integrys Energy Group.

Poor investment performance of retirement plan investments and other factors impacting retirement plan costs could unfavorably impact Integrys Energy Group’s liquidity and results of operations.

Integrys Energy Group has employee benefit plans that cover substantially all of its employees and retirees. Integrys Energy Group's cost of providing these benefit plans is dependent upon actual plan experience and assumptions concerning the future, such as earnings on and/or valuations of plan assets, discount rates, the level of interest rates used to measure the required minimum funding levels of the plans, future government regulation, and required or voluntary contributions to the plans. Depending upon the investment performance over time and other factors impacting its costs (as listed above), Integrys Energy Group could be required to make larger contributions in the future to fund these plans. These additional funding obligations could have a material adverse impact on Integrys Energy Group's cash flows, financial condition, and/or results of operations. Changes made to the plans may also impact current and future pension and other postretirement benefit costs.

Integrys Energy Group is subject to provisions that can limit merger and acquisition opportunities that could benefit its shareholders.

The Wisconsin Public Utility Holding Company Law precludes the acquisition of 10% or more of the voting shares of a holding company of a Wisconsin public utility unless the PSCW has first determined that the acquisition is in the best interests of utility customers, investors, and the public. Those interests may, to some extent, be mutually exclusive. This provision and other requirements of the Wisconsin Public Utility Holding Company Law may delay, or reduce the likelihood of, a sale or change of control thus reducing the likelihood that shareholders will receive a takeover premium for their shares.

Provisions of Integrys Energy Group's articles of incorporation and by-laws may delay or frustrate the removal of incumbent directors and may prevent or delay a merger, tender offer, or proxy contest involving Integrys Energy Group that is not approved by its board of directors, even if the shareholders believe that such events may be beneficial to Integrys Energy Group's interests. In addition, the Wisconsin Business Corporation Law contains provisions that may have the effect of delaying or making more difficult attempts by others to obtain control of Integrys Energy Group without the approval of its board of directors.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

# ITEM 2. PROPERTIES

## A. REGULATED

Electric Facilities

The following table summarizes information on the electric generation facilities of Integrys Energy Group, including owned and jointly owned facilities as of December 31, 2010:

| Type | Name | Location | Fuel | Rated Capacity (MW) (1) | |
|---|---|---|---|---|---|
| Steam | Columbia Units 1 and 2 | Portage, WI | Coal | 354.5 | (2) |
| | Edgewater Unit 4 | Sheboygan, WI | Coal | 98.0 | (2) |
| | Pulliam (4 units) | Green Bay, WI | Coal | 332.9 | |
| | Weston Units 1, 2, and 3 | Marathon County, WI | Coal | 460.9 | |
| | Weston Unit 4 | Marathon County, WI | Coal | 385.7 | (2) |
| Total Steam | | | | 1,632.0 | |
| | | | | | |
| Combustion Turbine and Diesel | De Pere Energy Center | De Pere, WI | Natural Gas | 169.6 | |
| | Eagle River | Eagle River, WI | Distillate Fuel Oil | 4.2 | |
| | Gladstone | Gladstone, MI | Oil | 18.2 | |
| | Juneau #31 | Adams County, WI | Distillate Fuel Oil | 6.2 | (2) |
| | Oneida Casino | Green Bay, WI | Distillate Fuel Oil | 3.5 | |
| | Portage | Houghton, MI | Oil | 18.4 | |
| | Pulliam #31 | Green Bay, WI | Natural Gas | 84.6 | |
| | West Marinette #31 | Marinette, WI | Natural Gas | 37.7 | |
| | West Marinette #32 | Marinette, WI | Natural Gas | 32.6 | |
| | West Marinette #33 | Marinette, WI | Natural Gas | 51.8 | (2) |
| | Weston #31 | Marathon County, WI | Natural Gas | 19.5 | |
| | Weston #32 | Marathon County, WI | Natural Gas | 48.1 | |
| Total Combustion Turbine and Diesel | | | | 494.4 | |
| | | | | | |
| Hydroelectric | Various | Michigan | Hydro | 20.1 | (3) |
| | Various | Wisconsin | Hydro | 67.8 | (4) |
| Total Hydroelectric | | | | 87.9 | |
| | | | | | |
| Wind | Kewaunee County | Wisconsin | Wind | 1.1 | |
| | Crane Creek | Iowa | Wind | 21.7 | |
| Total Wind | | | | 22.8 | |
| | | | | | |
| Total System | | | | 2,237.1 | |

(1) Based on capacity ratings for July 2011, which can differ from nameplate capacity, especially on wind projects. As a result of continually reaching demand peaks in the summer months, primarily due to air conditioning demand, the summer period is the most relevant for capacity planning purposes at Integrys Energy Group's electric segment.

(2)

These facilities are jointly owned by WPS and various other utilities. The capacity indicated for each of these units is equal to WPS's portion of total plant capacity based on its percent of ownership.

- Wisconsin Power and Light Company operates the Columbia and Edgewater units, and WPS holds a 31.8% ownership interest in these facilities.
- WPS operates the Weston 4 facility and holds a 70% ownership in this facility, while Dairyland Power Cooperative holds the remaining 30% interest.
- WRPC owns and operates the Juneau unit. WPS holds a 50% ownership interest in WRPC.
- At December 31, 2010, WPS operated the West Marinette 33 unit and held a 68% ownership interest in the facility, while Marshfield Electric and Water Department held the remaining 32% interest. On February 1, 2011, WPS purchased Marshfield Electric and Water Department's ownership interest and is now the sole owner of this facility.

(3) UPPCO sold the Cataract Hydroelectric Project to U.P. Hydro LLC., a wholly owned subsidiary of North American Hydro, on February 2, 2011. Cataract Hydroelectric accounted for 0.3 MW of the 20.1 MW hydroelectric generating capacity in Michigan.

(4) WRPC owns and operates the Castle Rock and Petenwell units. WPS holds a 50% ownership interest in WRPC; however, WPS is entitled to 66.7% of total capacity at Petenwell and Castle Rock.

As of December 31, 2010, Integrys Energy Group's electric utilities owned approximately 24,900 miles of electric distribution lines located in Michigan and Wisconsin and approximately 180 distribution substations.

Natural Gas Facilities

At December 31, 2010, Integrys Energy Group's natural gas properties were located in Illinois, Wisconsin, Minnesota, and Michigan, and consisted of the following:

- Approximately 22,000 miles of natural gas distribution mains,
- Approximately 1,030 miles of natural gas transmission mains,
- Approximately 290 natural gas distribution and transmission gate stations,
- Approximately 1.3 million natural gas lateral services,
- A 3.9 billion-cubic-foot underground natural gas storage field located in Michigan,
- A 38.2 billion-cubic-foot underground natural gas storage reservoir located in central Illinois, and
- A 2 billion-cubic-foot liquefied natural gas plant located in central Illinois.

General

Substantially all of Integrys Energy Group's utility plant at WPS, UPPCO, PGL, and NSG is subject to first mortgage liens.

## B. INTEGRYS ENERGY SERVICES

The following table summarizes information on the energy asset facilities owned by Integrys Energy Services as of December 31, 2010:

| Type | Name | Location | Fuel | Rated Capacity (MW) (1) | |
|---|---|---|---|---|---|
| Combined Cycle | Beaver Falls | Beaver Falls, NY | Gas/Oil | 79.1 | |
| | Combined Locks | Combined Locks, WI | Gas | 47.2 | (2) |
| | Syracuse | Syracuse, NY | Gas/Oil | 87.5 | |
| Total Combined Cycle | | | | 213.8 | |
| | | | | | |
| Steam | Westwood | Tremont, PA | Culm | 32.5 | |
| | | | | | |
| Reciprocating Engine | Winnebago | Rockford, IL | Landfill Gas | 6.4 | |
| | | | | | |
| Solar | Various | California | Solar Irradiance | 1.7 | |
| | Various | Connecticut | Solar Irradiance | 0.3 | |
| | Various | New Jersey | Solar Irradiance | 6.1 | |
| Total Solar | | | | 8.1 | |
| | | | | | |
| Total Energy Assets | | | | 260.8 | |
| | | | | | |
| | | | | Length of Pipeline | |

| | | | | | |
|---|---|---|---|---|---|
| | | | | (Miles) | |
| Landfill Gas Transportation | LGS | Brazoria County, TX | N/A | 33 miles | (3) |

(1) Based on summer rated capacity.
(2) Combined Locks has an additional five MW of capacity available at this facility through the lease of a steam turbine.
(3) LGS Renewables 1, LC, owns and operates the LGS facility, which transports and processes landfill gas.

## ITEM 3. LEGAL PROCEEDINGS

For information on material legal proceedings and matters related to Integrys Energy Group and its subsidiaries, see Note 15, "Commitments and Contingencies."

## ITEM 4. (REMOVED AND RESERVED)

# PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

### Common Stock Data

Integrys Energy Group's common stock is traded on the New York Stock Exchange under the ticker symbol "TEG." The transfer agent and registrar for Integrys Energy Group's common stock is American Stock Transfer & Trust Company, LLC, 6201 15th Avenue, Brooklyn, NY 11219. The quarterly high and low sales prices for Integrys Energy Group's common stock and the cash dividends per share declared for each quarter during the past two years were as follows:

| | 2010 | | | 2009 | | |
|---|---|---|---|---|---|---|
| Quarter | High | Low | Dividends | High | Low | Dividends |
| First | $47.67 | $40.53 | $0.68 | $45.10 | $19.44 | $0.68 |
| Second | 50.92 | 42.81 | 0.68 | 30.40 | 24.95 | 0.68 |
| Third | 52.74 | 42.92 | 0.68 | 36.75 | 28.31 | 0.68 |
| Fourth | 54.45 | 46.73 | 0.68 | 42.99 | 34.20 | 0.68 |

As of the close of business on February 21, 2011, there were 30,300 holders of record of Integrys Energy Group's common stock.

### Dividend Restrictions

Integrys Energy Group is a holding company and its ability to pay dividends is largely dependent upon the ability of its subsidiaries to pay dividends.

The PSCW has restricted WPS to paying normal dividends on its common stock of no more than 103% of the previous year's common stock dividend without the PSCW's approval. Integrys Energy Group is the sole holder of WPS's common stock. Integrys Energy Group's right to receive dividends on the common stock of WPS is also subject to the prior rights of WPS's preferred shareholders and to provisions in WPS's restated articles of incorporation, which limit the amount of common stock dividends that WPS may pay if its common stock and common stock surplus accounts constitute less than 25% of its total capitalization. These limitations are not expected to limit any dividend payments in the foreseeable future. At December 31, 2010, these limitations amounted to $1.4 million out of WPS's total retained earnings of $424.9 million. Consequently, at December 31, 2010, WPS had $423.5 million of retained earnings available for the payment of dividends.

UPPCO's indentures relating to its first mortgage bonds contain certain limitations on the payment of cash dividends on its common stock, which is held solely by Integrys Energy Group. At December 31, 2010, these restrictions amounted to $4.7 million out of UPPCO's total retained earnings of $57.9 million. Consequently, at December 31, 2010, UPPCO had $53.2 million of retained earnings available for the payment of common stock cash dividends.

NSG's long-term debt obligations contain provisions and covenants restricting the payment of cash dividends and the purchase or redemption of capital stock. At December 31, 2010, these restrictions amounted to $6.9 million out of NSG's total retained earnings of $70.2 million. Consequently, at December 31, 2010, NSG had $63.3 million of retained earnings available for the payment of dividends.

At December 31, 2010, Integrys Energy Group had $337.8 million of retained earnings available for the payment of dividends.  Except for the subsidiary restrictions described above, Integrys Energy Group does not have any dividend restrictions.

## Equity Compensation Plans

See Item 11, "Executive Compensation," for information regarding equity securities authorized for issuance under Integrys Energy Group’s equity compensation plans.

## Issuer Purchases of Equity Securities

Integrys Energy Group made no purchases of equity securities during the fourth quarter of 2010.

## ITEM 6. SELECTED FINANCIAL DATA

### INTEGRYS ENERGY GROUP, INC.
### COMPARATIVE FINANCIAL DATA AND OTHER STATISTICS (2006 TO 2010)

| As of or for Year Ended December 31 (Millions, except per share amounts, stock price, return on average equity, and number of shareholders and employees) | 2010 | 2009 (1) | 2008 (1) | 2007 (2) | 2006 (3) |
|---|---|---|---|---|---|
| Total revenues | $5,203.2 | $7,499.8 | $14,047.8 | $10,292.4 | $6,890.7 |
| Net income (loss) from continuing operations | 223.5 | (70.3) | 114.8 | 181.0 | 147.8 |
| Net income (loss) attributed to common shareholders | 220.9 | (69.6) | 116.5 | 251.3 | 155.8 |
| Total assets | 9,816.8 | 11,844.6 | 14,268.7 | 11,234.4 | 6,861.7 |
| Preferred stock of subsidiary | 51.1 | 51.1 | 51.1 | 51.1 | 51.1 |
| Long-term debt (excluding current portion) | 2,161.6 | 2,394.7 | 2,285.7 | 2,265.1 | 1,287.2 |
| Shares of common stock (less treasury stock and shares in deferred compensation trust) | | | | | |
| Outstanding | 77.4 | 76.0 | 76.0 | 76.0 | 43.1 |
| Average | 77.5 | 76.8 | 76.7 | 71.6 | 42.3 |
| Earnings (loss) per common share (basic) | | | | | |
| Net income (loss) from continuing operations | $2.85 | $(0.95) | $1.46 | $2.49 | $3.51 |
| Earnings (loss) per common share (basic) | 2.85 | (0.91) | 1.52 | 3.51 | 3.68 |
| Earnings (loss) per common share (diluted) | | | | | |
| Net income (loss) from continuing operations | 2.83 | (0.95) | 1.45 | 2.48 | 3.50 |
| Earnings (loss) per common share (diluted) | 2.83 | (0.91) | 1.51 | 3.50 | 3.67 |
| Dividends per common share declared | 2.72 | 2.72 | 2.68 | 2.56 | 2.28 |
| Stock price at year-end | $48.51 | $41.99 | $42.98 | $51.69 | $54.03 |
| Book value per share | $37.57 | $37.51 | $40.66 | $42.58 | $35.61 |

| | | | | | |
|---|---|---|---|---|---|
| Return on average equity | 7.7 % | (2.4 )% | 3.6 % | 8.5 % | 10.6 % |
| Number of common stock shareholders | 30,352 | 32,755 | 34,016 | 35,212 | 19,837 |
| Number of employees | 4,612 | 5,025 | 5,191 | 5,231 | 3,326 |

(1) Certain amounts have been retrospectively adjusted due to a change in accounting policy in 2010. See Note 1(d) "Change in Accounting Policy," for more information.
(2) Includes the impact of the PEC merger on February 21, 2007.
(3) Includes the impact of the acquisition of natural gas distribution operations by MGU on April 1, 2006, and MERC on July 1, 2006.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

INTRODUCTION

Integrys Energy Group is a diversified energy holding company with regulated natural gas and electric utility operations (serving customers in Illinois, Michigan, Minnesota, and Wisconsin), nonregulated energy operations, and an approximate 34% equity ownership interest in ATC (a federally regulated electric transmission company operating in Wisconsin, Michigan, Minnesota, and Illinois).

Strategic Overview

Integrys Energy Group's goal is to create long-term value for shareholders and customers through growth in its core regulated businesses. Integrys Energy Group also has a nonregulated energy services business segment that is smaller than it was historically with significantly reduced credit and collateral support requirements.

The essential components of Integrys Energy Group's business strategy are:

Maintaining and Growing a Strong Regulated Utility Base – A strong regulated utility base is essential to maintaining a strong balance sheet, predictable cash flows, the desired risk profile, attractive dividends, and quality credit ratings. This is critical to Integrys Energy Group's success as a strategically focused regulated business. Integrys Energy Group believes the following projects have helped, or will help, maintain and grow its regulated utility base and meet its customers' needs:

- An accelerated annual investment in natural gas distribution facilities (primarily replacement of cast iron mains) at PGL.

- WPS's continued investment in environmental projects to improve air quality and meet the requirements set by environmental regulators. Capital projects to construct and/or upgrade equipment to meet or exceed required environmental standards are planned each year.

- Integrys Energy Group's approximate 34% ownership interest in ATC, a transmission company that had over $2.9 billion of transmission assets at December 31, 2010. ATC plans to invest approximately $3.4 billion during the next ten years. Although ATC's equity requirements to fund its capital investments will primarily be met by earnings reinvestment, Integrys Energy Group plans to continue to fund its share of the equity portion of future ATC growth as necessary.

For more detailed information on Integrys Energy Group's capital expenditure program, see "Liquidity and Capital Resources, Capital Requirements."

Operating a Nonregulated Energy Services Business Segment with a Controlled Risk and Capital Profile – Through its nonregulated Integrys Energy Services subsidiary, Integrys Energy Group provides retail natural gas and electric products to end-use customers in the northeast quadrant of the United States. Integrys Energy Group has repositioned this subsidiary from a focus on significant growth in wholesale and retail electric markets across the United States and Canada, to a focus on operating within select retail electric and natural gas markets in its current market footprint where it has experience and believes it will have the most success growing its recurring customer based business. The current strategy is intended to result in more dependable cash and earnings contributions with a controlled risk and capital profile. In addition, Integrys Energy Services continues to invest in and promote renewable energy in the United States. Clean, renewable, and efficient energy sources are developed, acquired, owned, and operated by Integrys Energy Services. Integrys Energy Services assists customers with selecting an energy solution that meets their needs and collaborates with energy developers of wholesale energy projects to overcome challenges with integrating the technical, regulatory, and financial aspects of their projects.

Integrating Resources to Provide Operational Excellence – Integrys Energy Group is committed to integrating resources of all its businesses, while meeting all applicable legal and regulatory requirements. This will provide the best value to customers and shareholders by leveraging the individual capabilities and expertise of each business and lowering costs. "Operational Excellence" initiatives were implemented to encourage top performance in the areas of project management, process improvement, contract administration, and compliance in order to reduce costs and manage projects and activities within appropriate budgets, schedules, and regulations.

Placing Strong Emphasis on Asset and Risk Management – Integrys Energy Group's asset management strategy calls for the continuous assessment of existing assets, the acquisition of assets, and contractual commitments to obtain resources that complement its existing business and strategy. The goal is to provide the most efficient use of resources while maximizing return and maintaining an acceptable risk profile. This strategy focuses on acquiring assets consistent with strategic plans and disposing of assets, including property, plant, and equipment and entire business units, which are no longer strategic to ongoing operations, are not performing as needed, or have an unacceptable risk profile. Integrys Energy Group maintains a portfolio approach to risk and earnings.

Integrys Energy Group's risk management strategy includes the management of market, credit, liquidity, and operational risks through the normal course of business. Forward purchases and sales of electric capacity, energy, natural gas, and other commodities and the use of derivative financial instruments, including commodity swaps and options, allow for opportunities to reduce the risk associated with price movement in a volatile energy market. Each business unit manages the risk profile related to these instruments consistent with Integrys Energy Group's risk management policies, which are approved by the Board of Directors. The Corporate Risk Management Group, which reports through the Chief Financial Officer, provides corporate oversight.

Continuing Emphasis on Safe, Reliable, Competitively Priced, and Environmentally Sound Energy and Energy Related Services – Integrys Energy Group's mission is to provide customers with the best value in energy and energy related services. By effectively operating a mixed portfolio of generation assets and investing in new generation and natural gas distribution assets, while maintaining or exceeding environmental standards, Integrys Energy Group is able to provide a safe, reliable, value-priced service to its customers. Integrys Energy Group concentrates its efforts on improving and operating efficiently in order to reduce costs and maintain a low risk profile. Integrys Energy Group actively evaluates opportunities for adding more renewable generation to provide additional environmentally sound energy to its portfolio. Ensuring continued reliability for its customers, Integrys Energy Group is effectively operating a mixed portfolio of generation assets and investing in new generation and distribution assets.

## RESULTS OF OPERATIONS

### Earnings Summary

| (Millions, except per share amounts) | Year Ended December 31 2010 | 2009* | 2008* | Change in 2010 Over 2009 | Change in 2009 Over 2008 |
|---|---|---|---|---|---|
| Natural gas utility operations | $84.0 | $(172.1) | $84.5 | N/A | N/A |
| Electric utility operations | 109.8 | 88.9 | 92.6 | 23.5 % | (4.0)% |
| Integrys Energy Services operations | 3.3 | 3.8 | (71.4) | (13.2)% | N/A |
| Electric transmission investment | 46.2 | 45.5 | 39.7 | 1.5 % | 14.6 % |
| Holding company and other operations | (22.4) | (35.7) | (28.9) | (37.3)% | 23.5 % |
| Net income (loss) attributed to common shareholders | $220.9 | $(69.6) | $116.5 | N/A | N/A |
| | | | | | |
| Basic earnings (loss) per share | $2.85 | $(0.91) | $1.52 | N/A | N/A |
| Diluted earnings (loss) per share | $2.83 | $(0.91) | $1.51 | N/A | N/A |
| | | | | | |
| Average shares of common stock | | | | | |
| Basic | 77.5 | 76.8 | 76.7 | 0.9 % | 0.1 % |
| Diluted | 78.0 | 76.8 | 77.0 | 1.6 % | (0.3)% |

* Certain amounts have been retrospectively adjusted due to a change in accounting policy in the fourth quarter of 2010. See Note 1(d), "Change in Accounting Policy," for more information.

### 2010 Compared with 2009

Integrys Energy Group recognized net income attributed to common shareholders of $220.9 million ($2.83 diluted earnings per share) in 2010 compared with a net loss attributed to common shareholders of $69.6 million ($0.91 net loss per share) in 2009. The primary driver of the $290.5 million increase in earnings was an after-tax noncash goodwill impairment loss of $248.8 million recorded in 2009, compared with no goodwill impairment losses in 2010. Other factors contributing to the increase were the combined approximate $69 million after-tax positive impact on margins of electric and natural gas distribution rate increases effective in 2010, and a $22.5 million after-tax reduction in restructuring expenses year over year. These increases in earnings were partially offset by after-tax impairment charges of $25.9 million in 2010 related to three natural gas-fired generation plants at Integrys Energy Services.

### 2009 Compared with 2008

Integrys Energy Group recognized a net loss attributed to common shareholders of $69.6 million ($0.91 net loss per share) in 2009 compared with net income attributed to common shareholders of $116.5 million ($1.51 diluted earnings per share) in 2008. The primary drivers of the $186.1 million decrease in earnings were a $242.3 million after-tax year-over-year increase in noncash goodwill impairment losses, $27.2 million of after-tax restructuring charges recorded in 2009, and $17.3 million of after-tax net losses on dispositions in 2009 related to the Integrys Energy Services strategy change. These decreases in earnings were partially offset by a $127.3 million after-tax increase in margins at Integrys Energy Services, primarily due to the positive year-over-year impact of noncash inventory valuation adjustments recorded in prior periods, partially offset by noncash accounting losses in 2009 versus noncash accounting gains in 2008 due to derivative fair value adjustments.

Regulated Natural Gas Utility Segment Operations

| | Year Ended December 31 | | | | |
|---|---|---|---|---|---|
| | 2010 | 2009 | 2008 | Change in 2010 Over 2009 | Change in 2009 Over 2008 |
| Revenues | $2,057.2 | $2,237.5 | $3,025.9 | (8.1)% | (26.1)% |
| Purchased natural gas costs | 1,152.0 | 1,382.0 | 2,147.7 | (16.6)% | (35.7)% |
| Margins | 905.2 | 855.5 | 878.2 | 5.8% | (2.6)% |
| Operating and maintenance expense | 542.1 | 532.6 | 539.1 | 1.8% | (1.2)% |
| Goodwill impairment loss | - | 291.1 | 6.5 | (100.0)% | 4,378.5% |
| Restructuring expense | (0.2) | 6.9 | - | N/A | N/A |
| Depreciation and amortization expense | 130.9 | 106.1 | 108.3 | 23.4% | (2.0)% |
| Taxes other than income taxes | 34.4 | 33.4 | 32.1 | 3.0% | 4.0% |
| Operating income (loss) | 198.0 | (114.6) | 192.2 | N/A | N/A |
| Miscellaneous income | 1.6 | 3.1 | 7.0 | (48.4)% | (55.7)% |
| Interest expense | (49.7) | (52.2) | (56.6) | (4.8)% | (7.8)% |
| Other expense | (48.1) | (49.1) | (49.6) | (2.0)% | (1.0)% |
| Income (loss) before taxes | $149.9 | $(163.7) | $142.6 | N/A | N/A |
| Throughput in therms | | | | | |
| Residential | 1,496.4 | 1,602.8 | 1,708.9 | (6.6)% | (6.2)% |
| Commercial and industrial | 455.5 | 501.4 | 550.8 | (9.2)% | (9.0)% |
| Interruptible | 39.8 | 51.3 | 60.1 | (22.4)% | (14.6)% |
| Interdepartmental | 13.9 | 9.5 | 28.6 | 46.3% | (66.8)% |
| Transport | 1,728.4 | 1,641.6 | 1,834.0 | 5.3% | (10.5)% |
| Total throughput in therms | 3,734.0 | 3,806.6 | 4,182.4 | (1.9)% | (9.0)% |
| Weather | | | | | |
| Average heating degree days | 6,440 | 7,061 | 7,257 | (8.8)% | (2.7)% |

2010 Compared with 2009

Revenues

Regulated natural gas utility segment revenues decreased $180.3 million year over year, driven by:

- An approximate $132 million decrease in revenues as a result of the 1.9% lower natural gas throughput volumes, related to:
  - An approximate $76 million decrease driven by lower weather-normalized volumes. Residential customer volumes decreased, which Integrys Energy Group attributes to energy conservation, efficiency efforts, and general

economic conditions. In addition, some former MGU residential and small commercial and industrial retail customers have become transportation customers under a Michigan customer choice program, which resulted in reduced revenues of approximately $6 million in 2010 related to the pass-through of the cost of natural gas but had no impact on margins. These decreases were partially offset by a year-over-year net increase in commercial and industrial sales volumes for both retail and transportation customers, driven by certain transportation customers of MERC and MGU.

- An approximate $66 million decrease as a result of warmer year-over-year weather during the heating season, as evidenced by the 8.8% decrease in average heating degree days.

- Partially offsetting these decreases was the approximate $10 million positive year-over-year impact of decoupling mechanisms for residential, small commercial and industrial, and transportation customers. Under decoupling, certain of Integrys Energy Group's regulated natural gas utilities are allowed to defer the difference between the actual and rate case authorized delivery charge components of margin from certain customers and adjust future rates in accordance with rules applicable to each jurisdiction. The decoupling mechanism for WPS's natural gas utility includes an annual $8.0 million cap for the deferral of any excess or shortfall from the rate case authorized margin. This cap was reached in the first quarter of 2010 but was not reached in 2009.

· An approximate $127 million decrease in revenues as a result of an approximate 9% year-over-year decrease in the average per-unit cost of natural gas sold. For all of Integrys Energy Group's regulated natural gas utilities, prudently incurred natural gas commodity costs are passed directly through to customers in current rates.

· An approximate $18 million net decrease in revenues driven by lower recovery of approximately $25 million of environmental cleanup expenditures related to former manufactured gas plant sites, partially offset by an approximate $7 million increase related to recoveries received in 2010 under the PGL and NSG bad debt riders. These amounts were offset by a net decrease in operating and maintenance expense resulting from lower net amortization of the related regulatory assets and, therefore, had no impact on earnings. Recoveries under these riders represent net billings to customers of the excess or deficiency of actual 2008 and 2009 bad debt expense over bad debt expense reflected in utility rates during those same periods. See Note 24, "Regulatory Environment," for more information on the PGL and NSG bad debt riders.

· Partially offsetting these decreases was the approximate $96 million positive impact of natural gas distribution rate increases. These rate increases were necessary, in part, to recover higher operating expenses (as discussed below). See Note 24, "Regulatory Environment," for more information on these rate increases.

- The rate increases at PGL and NSG had an approximate $77 million positive impact on revenues.

- The rate increase at WPS had an approximate $13 million positive impact on revenues.

- The rate increase at MGU had an approximate $3 million positive impact on revenues.

- A rate increase at MERC related to its conservation improvement program had an approximate $3 million positive impact on revenues. This amount is offset by a corresponding increase in operating and maintenance expense and, therefore, had no impact on earnings.

Margins

Regulated natural gas utility segment margins increased $49.7 million year over year, driven by the approximate $96 million positive impact of the rate increases, partially offset by:

- An approximate $28 million decrease in margins resulting from lower natural gas throughput volumes, resulting from:

  - An approximate $19 million decrease related to warmer year-over-year weather during the heating season.

  - An approximate $19 million decrease related to lower weather-normalized volumes, primarily attributed to residential customer conservation, efficiency efforts, and general economic conditions, partially offset by the favorable net impact of increased commercial and industrial sales volumes for certain retail and transportation customers of MERC and MGU.

- Partially offsetting these decreases was the approximate $10 million positive impact from decoupling mechanisms in place at certain of Integrys Energy Group's regulated natural gas utilities.

· An approximate $18 million net decrease in margins driven by lower recovery of environmental cleanup expenditures related to former manufactured gas plant sites, partially offset by an increase in margins related to recoveries received under the PGL and NSG bad debt riders. These amounts were offset by a net decrease in operating and maintenance expense resulting from lower net amortization of the related regulatory assets and, therefore, had no impact on earnings.

Operating Income (Loss)

Operating income at the regulated natural gas utility segment increased $312.6 million year over year. This increase was primarily driven by the positive year-over-year impact of a $291.1 million noncash goodwill impairment loss that was recorded in the first quarter of 2009. Also contributing to the increase was the $49.7 million increase in the natural gas margins discussed above, partially offset by a $28.2 million increase in other operating expenses. See Note 9, "Goodwill and Other Intangible Assets," for information related to the goodwill impairment loss recorded in 2009.

The $28.2 million year-over-year increase in other operating expenses primarily related to:

· A $24.8 million increase in depreciation and amortization expense, primarily due to the ICC's rate order for PGL and NSG, effective January 28, 2010, which allows earlier recovery in rates for net dismantling costs by including them as a component of depreciation rates applied to natural gas distribution assets. The increase also includes a $2.5 million write-off of MGU assets for which rate recovery is currently being contested.

· A $12.9 million increase in expenses related to energy conservation programs and enhanced efficiency initiatives.

· A $9.8 million increase in employee benefit costs, primarily driven by an increase in other postretirement benefit costs.

· A $7.4 million increase in asset usage charges from IBS related to implementation of both a work asset management system for natural gas operations and a newer version of an Enterprise Resource Planning system for finance and supply chain services.

· A $4.9 million increase in stock-based compensation expense. See Note 20, "Stock-Based Compensation," for more information.

· These increases were partially offset by:

- An approximate $18 million net decrease due to approximately $25 million of lower amortization of the regulatory asset related to environmental cleanup expenditures for manufactured gas plant sites, partially offset by approximately $7 million of amortization related to the regulatory assets recorded as a result of the PGL and NSG bad debt riders. This net decrease was passed through to customers in rates and, therefore, had no impact on earnings.

- A $7.1 million decrease in restructuring expenses recorded in 2009 related to a reduction in workforce. See Note 3, "Restructuring Expense," for more information.

- A $6.1 million decrease in labor costs as a result of the reduction in workforce and company-wide furloughs implemented as a part of previously announced cost management efforts.

2009 Compared with 2008

Revenues

Regulated natural gas utility segment revenues decreased $788.4 million, driven by:

- An approximate $648 million decrease in revenues as a result of an approximate 30% decrease in the average per-unit cost of natural gas sold by the regulated natural gas utilities during 2009 compared with 2008. For all of Integrys Energy Group's regulated natural gas utilities, prudently incurred natural gas commodity costs are passed directly through to customers in current rates.

- An approximate $166 million decrease in revenues as a result of lower year-over-year natural gas throughput volumes, driven by:

  - An approximate $83 million decrease related to lower weather-normalized volumes, including residential customer volumes, resulting from customer conservation and efficiency efforts. Lower volumes were also driven by decreased commercial and industrial customer volumes resulting from reduced demand related to changes in customers' plant operations and a decline in customer base at PGL and MGU, both of which Integrys Energy Group attributed to the general economic slowdown.

  - An approximate $70 million decrease as a result of warmer year-over-year weather during the heating season as indicated by the 2.7% decrease in average heating degree days.

  - An approximate $19 million decrease related to a reduction in volumes sold to the electric utility segment driven by the availability of lower cost power from MISO, resulting in a decrease in the need for the electric utility to run its natural gas-fired peaking generation units.

  - This decrease in revenues was partially offset by the $6 million positive impact of decoupling mechanisms that were first effective for PGL and NSG on March 1, 2008, and for WPS on January 1, 2009. Under decoupling, these utilities are allowed to defer the difference between the actual and rate case authorized delivery charge components of margin from certain customers and adjust future rates in accordance with rules applicable to each jurisdiction.

- An approximate $20 million year-over-year net decrease in revenues from lower recovery of environmental cleanup expenditures at PGL and NSG related to former manufactured gas plant sites, partially offset by higher recovery of EEP expenses. The EEP program was established in the 2008 PGL and NSG rate cases and is designed to encourage energy efficiency initiatives.

- The decrease in revenues was partially offset by the approximate $29 million year-over-year net positive impact of natural gas distribution rate cases and changes in rate design at the regulated natural gas utilities. See Note 24, "Regulatory Environment," for more information on these rate cases.

- Effective January 14, 2009, MGU received a final rate order from the MPSC for a natural gas distribution rate increase. On June 29, 2009, MERC received a final rate order granting a natural gas distribution rate increase. Prior to this final order, MERC had been granted interim rate relief effective October 1, 2008. Together, these rate increases had an approximate $19 million positive impact on revenue.

- In 2009, PGL and NSG received the full impact of their 2008 natural gas distribution rate orders, which were effective February 14, 2008, and drove an approximate $5 million increase in revenue year over year.

- Effective January 1, 2009, the PSCW required WPS to change its retail natural gas distribution rate design which incorporates higher volumetric rates and lower fixed customer charges. In 2009, revenue increased approximately $5 million related to this change in rate design.

Margins

Regulated natural gas utility segment margins decreased $22.7 million, driven by:

· An approximate $27 million year-over-year decrease in margins resulting from the 9.0% decrease in natural gas throughput volumes attributed to the negative impact of the general economic slowdown, customer conservation and efficiency efforts, and warmer year-over-year weather. This decrease in margins includes the impact of decoupling mechanisms that were first effective for PGL and NSG on March 1, 2008, and for WPS on January 1, 2009. The decoupling mechanism for WPS's natural gas utility includes an annual $8.0 million cap for the deferral of any excess or shortfall from the rate case authorized margin. Approximately $7 million of additional margin was recognized at WPS due to a shortfall from the rate case authorized margin during 2009.

· An approximate $20 million year-over-year net decrease in margins due to lower recovery of environmental cleanup expenditures at PGL and NSG related to former manufactured gas plant sites, partially offset by an increase in recovery of EEP expenses. This decrease in margin was offset by a net decrease in operating expense from both the amortization of the related regulatory asset and EEP expenses and, therefore, had no impact on earnings.

· An approximate $2 million year-over-year decrease in margins at MGU related to an adjustment in the third quarter of 2008 for recovery of natural gas costs in a MPSC proceeding.

· The decrease in margins was partially offset by the approximate $29 million net positive year-over-year impact of rate orders and impacts of rate design changes at the regulated natural gas utilities.

Operating Income (Loss)

Operating results at the regulated natural gas utility segment decreased $306.8 million, from operating income of $192.2 million in 2008, to an operating loss of $114.6 million in 2009. This decrease was primarily driven by a year-over-year increase in noncash goodwill impairment losses of $284.6 million and the $22.7 million decrease in natural gas margin, partially offset by a $0.5 million decrease in other operating expenses. See Note 9, "Goodwill and Other Intangible Assets," for information related to the goodwill impairment losses recorded in 2009 and 2008.

The year-over-year decrease in other operating expenses primarily related to:

· An approximate $20 million net decrease in amortization of the regulatory asset related to environmental cleanup expenditures of manufactured gas plant sites, partially offset by an increase in EEP expenses. Both of these costs were recovered from customers in rates.

·

A $17.7 million decrease in bad debt expense driven by the impact lower energy prices had on overall accounts receivable balances and the implementation of bad debt expense tracking mechanisms at PGL, NSG, and MGU. PGL and NSG elected during the third quarter of 2009, under a new Illinois state law, to file for recovery from or refund to customers the difference between actual bad debt expense reported as a component of earnings and the bad debt expense included in utility rates retroactive to January 1, 2008. Bad debt expense also decreased as a result of MGU's rate order effective January 1, 2010, which established a bad debt expense tracking mechanism that allows for the deferral and subsequent recovery or refund of 80% of the difference between actual bad debt write-offs (net of recoveries) and bad debt expense included in utility rates. The bad debt mechanism allowed recovery of a portion of the December 31, 2009 accounts receivable reserve representing future bad debt write-offs. The decrease in bad debt expense attributed to the implementation of bad debt expense tracking mechanisms at the natural gas utilities was $9.3 million.

· These decreases were partially offset by:

- A $13.4 million increase in employee benefit costs, partially related to an increase in pension expense resulting from negative pension investment returns in 2008, as well as higher health care expenses in 2009.

- Restructuring expenses of $6.9 million related to a reduction in workforce. See Note 3, "Restructuring Expense," for more information.

- A $5.5 million increase in natural gas maintenance costs, primarily related to increased system inspection and maintenance requirements.

- A $5.0 million increase in expenses related to workers compensation claims.

- A $3.0 million charge related to an expected settlement with the ICC at PGL and NSG related to fiscal years 2001 through 2004 natural gas costs. See Note 15, "Commitments and Contingencies," for more information.

- A $2.5 million increase in amortization of a regulatory asset related to conservation program initiatives.

Regulated Electric Utility Segment Operations

| | Year Ended December 31 | | | | |
|---|---|---|---|---|---|
| | 2010 | 2009 | 2008 | Change in 2010 Over 2009 | Change in 2009 Over 2008 |
| Revenues | $1,338.9 | $1,301.6 | $1,328.9 | 2.9 % | (2.1 )% |
| Fuel and purchased power costs | 563.9 | 584.5 | 651.5 | (3.5 )% | (10.3 )% |
| Margins | 775.0 | 717.1 | 677.4 | 8.1 % | 5.9 % |
| | | | | | |
| Operating and maintenance expense | 417.2 | 392.0 | 375.3 | 6.4 % | 4.4 % |
| Restructuring expense | (0.3 ) | 8.6 | - | N/A | N/A |
| Depreciation and amortization expense | 94.7 | 90.3 | 84.3 | 4.9 % | 7.1 % |
| Taxes other than income taxes | 45.6 | 46.6 | 44.3 | (2.1 )% | 5.2 % |
| | | | | | |
| Operating income | 217.8 | 179.6 | 173.5 | 21.3 % | 3.5 % |
| | | | | | |
| Miscellaneous income | 1.5 | 4.8 | 6.0 | (68.8 )% | (20.0 )% |
| Interest expense | (43.9 ) | (41.6 ) | (36.7 ) | 5.5 % | 13.4 % |
| Other expense | (42.4 ) | (36.8 ) | (30.7 ) | 15.2 % | 19.9 % |
| | | | | | |
| Income before taxes | $175.4 | $142.8 | $142.8 | 22.8 % | - % |
| | | | | | |
| Sales in kilowatt-hours | | | | | |
| Residential | 3,114.3 | 3,043.0 | 3,064.5 | 2.3 % | (0.7 )% |

| | | | | | |
|---|---|---|---|---|---|
| Commercial and industrial | 8,439.6 | 8,155.5 | 8,632.8 | 3.5 % | (5.5 )% |
| Wholesale | 4,994.7 | 5,079.1 | 4,764.6 | (1.7 )% | 6.6 % |
| Other | 39.1 | 40.0 | 42.6 | (2.3 )% | (6.1 )% |
| Total sales in kilowatt-hours | 16,587.7 | 16,317.6 | 16,504.5 | 1.7 % | (1.1 )% |
| | | | | | |
| Weather – WPS: | | | | | |
| Heating degree days | 7,080 | 7,962 | 7,969 | (11.1 )% | (0.1 )% |
| Cooling degree days | 616 | 274 | 464 | 124.8 % | (40.9 )% |
| | | | | | |
| Weather – UPPCO: | | | | | |
| Heating degree days | 8,002 | 9,317 | 9,348 | (14.1 )% | (0.3 )% |
| Cooling degree days | 301 | 99 | 138 | 204.0 % | (28.3 )% |

2010 Compared with 2009

Revenues

Regulated electric utility segment revenues increased $37.3 million year over year, driven by:

- The approximate $21 million combined positive impact of retail electric rate increases at both WPS and UPPCO, effective January 1, 2010. These rate increases were necessary, in part, for recovery of higher operating expenses (as discussed below).

- An approximate $16 million increase in revenues due to a 7.5% increase in sales volumes to large commercial and industrial customers at WPS, primarily related to changes in the business operations of these customers year over year.

- An approximate $13 million increase in revenues due to a 2.7% increase in sales volumes to residential customers and a 0.9% increase in sales volumes to small commercial and industrial customers at WPS, primarily related to warmer year-over-year weather during the cooling season as evidenced by the increase in cooling degree days.

- An approximate $4 million increase in opportunity sales at WPS, made possible by the availability of low-cost energy from Weston 4.

- These increases in regulated electric utility segment revenues were partially offset by an approximate $18 million decrease in revenues from wholesale customers at WPS, primarily due to lower fuel costs. Fuel costs are passed directly through to wholesale customers in rates.

Margins

Regulated electric utility segment margins increased $57.9 million year over year, driven by:

- An approximate $26 million increase in margins driven by lower fuel and purchased power costs incurred during 2010 as compared with authorized fuel and purchased power cost recovery rates.

- The approximate $21 million combined positive impact of retail electric rate increases at both WPS and UPPCO, effective January 1, 2010.

- An approximate $7 million increase in margins due to a 2.7% increase in sales volumes to residential customers at WPS, primarily related to warmer year-over-year weather during the cooling season, as evidenced by the increase in cooling degree days. Margins were impacted by the year-over-year increase in sales volumes because WPS reached the annual $14.0 million electric decoupling cap in the second quarter of 2010 and 2009 and remained over the cap through the end of both years. Therefore, no additional decoupling deferral was allowed for additional shortfalls from authorized margin for the remainder of both years. Under decoupling, WPS is allowed to defer (up to the established cap) the difference between its actual margin and the rate case authorized margin recognized from residential and small commercial and industrial customers.

- An approximate $7 million increase in margins due to a 7.5% increase in sales volumes to large commercial and industrial customers at WPS, primarily related to changes in the business operations of these customers year over year.

- These increases in regulated electric utility segment margins were partially offset by an approximate $2 million decrease in margins from WPS's wholesale customers, primarily due to a decrease in sales volumes.

Operating Income

Operating income at the regulated electric utility segment increased $38.2 million year over year, driven by the $57.9 million increase in margins, partially offset by a $19.7 million increase in operating expenses.

The year-over-year increase in operating expenses was the result of:

- A $13.9 million increase in electric transmission expense.
- A $12.7 million increase in customer assistance expense related to payments made to the Focus on Energy program, which helps residents and businesses install cost-effective, energy-efficient, and renewable energy products.
- A $4.4 million increase in depreciation and amortization expense, primarily related to the Crane Creek Wind Farm being placed in service for accounting purposes in December 2009.
- A $3.9 million increase in stock-based compensation expense. See Note 20, "Stock-Based Compensation," for more information.
- A $3.6 million increase in employee benefit costs, primarily related to an increase in pension and other postretirement benefit expenses, driven by the amortization of negative investment returns on plan assets from prior years.
- These increases in regulated electric utility operating expenses were partially offset by:
  - An $8.9 million year-over-year decrease in restructuring expenses related to a reduction in workforce. See Note 3, "Restructuring Expense," for more information.
  - A $6.2 million decrease in labor costs, driven by the reduction in workforce and company-wide furloughs implemented as part of previously announced cost management efforts.
  - A $2.1 million decrease in electric maintenance expense at WPS, primarily related to a greater number of planned outages at its generation plants during 2009 compared with 2010.

Other Expense

Other expense at the regulated electric utility segment increased $5.6 million year over year, driven by a decrease in AFUDC, primarily related to the construction of the Crane Creek Wind Farm in 2009.

2009 Compared with 2008

Revenues

Regulated electric utility segment revenues decreased $27.3 million year over year, driven by:

- A 5.5% decrease in commercial and industrial sales volumes and a 0.7% decrease in residential sales volumes, which resulted in an approximate $23 million year-over-year decrease in revenues, after the impact of decoupling. The primary drivers of the decrease were:
  - An approximate $31 million year-over-year decrease due to lower demand related to changes in commercial and industrial customers' plant operations, which Integrys Energy Group attributed mainly to the general economic slowdown.
  - An approximate $6 million decrease primarily related to cooler year-over-year weather during the cooling season as evidenced by the decrease in cooling degree days at both WPS and UPPCO.

- These decreases in volumes were partially offset by the $14.0 million impact that decoupling, which went into effect on January 1, 2009, had on WPS's revenue. The four-year pilot program for electric decoupling has an annual $14.0 million cap for the deferral of any excess or shortfall from the rate case authorized margin. This cap was reached during the second quarter of 2009; therefore, no additional decoupling deferral was allowed for additional shortfalls from authorized margin for the second half of the year.

· An approximate $22 million year-over-year reduction in revenues related to refunds due to customers in both 2009 and 2008 related to WPS's over-collection of fuel costs. On April 23, 2009, the PSCW made 2009 fuel cost recovery subject to refund, effective April 25, 2009, as actual and projected fuel costs for the remainder of the year were estimated to be below the 2% fuel window. See Note 24, "Regulatory Environment," for more information on WPS's fuel window.

· An approximate $14 million year-over-year decrease in opportunity sales driven by lower demand and the availability of lower cost power from the MISO market.

· These decreases in regulated electric utility segment revenues were partially offset by:

- An approximate $19 million increase in revenues driven by higher wholesale volumes due to an increase in contracted sales volumes to a large wholesale customer and an increase in the wholesale demand rate, effective January 1, 2009, to recover costs related to Weston 4.

- An approximate $15 million increase in revenues from the combined effect of the July 4, 2008 fuel surcharge, a portion of which was incorporated into WPS's 2009 non-fuel base retail electric rates, and the full year's benefit of the 2008 retail electric rate increase, effective January 16, 2008, for WPS.

Margins

The regulated electric utility segment margins increased $39.7 million year over year, driven by:

· An approximate $20 million year-over-year increase in margins from wholesale customers related to increases in contracted sales volumes with an existing customer and an increase in the wholesale demand rate, effective January 1, 2009, to recover costs related to Weston 4.

· An approximate $14 million year-over-year increase in margins from the combined effect of the July 4, 2008 fuel surcharge, a portion of which was incorporated into WPS's 2009 non-fuel base retail electric rates, and the full year's benefit of the 2008 retail electric rate increase, effective January 16, 2008, for WPS.

· An approximate $11 million year-over-year increase in WPS's regulated electric utility margins due to fuel and purchased power costs that were approximately $12 million lower than what was recovered in rates during 2009, compared with fuel and purchased power costs that were approximately $1 million lower than what was recovered in rates during

2008.

- The increase in margins was partially offset by an approximate $4 million year-over-year decrease in margin, after the impact of the WPS decoupling mechanism, caused by a 4.3% year-over-year decrease in sales volumes to residential and commercial and industrial customers. The $14.0 million impact of decoupling partially offset the approximate $18 million decrease in margins due to lower sales volumes, which was attributed to the general economic slowdown and cooler year-over-year weather during the cooling season.

Operating Income

Operating income at the regulated electric utility segment increased $6.1 million year over year, driven by the $39.7 million increase in margins, partially offset by a $33.6 million increase in operating expenses.

The year-over-year increase in operating expenses was driven by:

- $8.6 million in restructuring expenses related to a reduction in workforce. See Note 3, "Restructuring Expense," for more information.
- An $8.2 million increase in electric maintenance expenses at WPS, primarily related to a greater number of planned outages at the generation plants during 2009, compared with 2008.
- An $8.1 million increase in employee benefit costs, primarily related to an increase in pension expense driven partially by negative pension investment returns in 2008, as well as higher health care expenses in 2009.
- A $5.6 million increase in depreciation and amortization expense at WPS, primarily related to Weston 4 being placed in service for accounting purposes in April 2008.

Other Expense

Other expense at the regulated electric utility segment increased $6.1 million year over year, driven by:

- A $4.9 million increase in interest expense, primarily related to increased long-term borrowings at WPS in December 2008. The additional borrowings were utilized to fund various construction projects, most notably the Crane Creek wind generation project in Iowa.
- A $2.5 million decrease in interest earned on the transmission facilities WPS funded on ATC's behalf. WPS was reimbursed by ATC for these transmission facilities in April 2008.

Electric Transmission Investment Segment Operations

2010 Compared with 2009

Miscellaneous Income

Miscellaneous income at the electric transmission investment segment increased $2.3 million during 2010, compared with 2009, due to an increase in income from Integrys Energy Group's approximate 34% ownership interest in ATC. The increase in income was driven by returns earned by ATC on increased investment in transmission equipment and facilities for improved reliability.

2009 Compared with 2008

Miscellaneous Income

Miscellaneous income at the electric transmission investment segment increased $9.2 million during 2009 compared with 2008, due to an increase in income from Integrys Energy Group's approximate 34% ownership interest in ATC. The increase in income was driven by returns earned by ATC on increased investment in transmission equipment and facilities for improved reliability.

Integrys Energy Services Nonregulated Segment Operations

| (Millions, except natural gas sales volumes) | Year Ended December 31 2010 | | 2009 (3) | 2008 | Change in 2010 Over 2009 | Change in 2009 Over 2008 |
|---|---|---|---|---|---|---|
| Revenues | $1,823.7 | | $3,994.0 | $9,735.2 | (54.3)% | (59.0)% |
| Cost of fuel, natural gas, and purchased power | 1,614.3 | | 3,696.1 | 9,649.5 | (56.3)% | (61.7)% |
| Margins | 209.4 | | 297.9 | 85.7 | (29.7)% | 247.6% |
| Margin Detail | | | | | | |
| Realized retail electric margins | 85.4 | (1) | 82.0 | 62.3 | 4.1% | 31.6% |
| Realized wholesale electric margins | (8.2) | (2) | 40.3 | 30.9 | N/A | 30.4% |
| Realized energy asset margins | 34.5 | | 37.9 | 28.5 | (9.0)% | 33.0% |
| Fair value adjustments | 36.0 | | 29.9 | (137.4) | 20.4% | N/A |
| Electric and other margins | 147.7 | | 190.1 | (15.7) | (22.3)% | N/A |
| Realized retail natural gas margins | 50.0 | | 68.7 | 51.5 | (27.2)% | 33.4% |
| Realized wholesale natural gas margins | (3.3) | | 40.8 | 64.1 | N/A | (36.3)% |
| Lower-of-cost-or-market inventory adjustments | 6.8 | | 155.4 | (167.3) | (95.6)% | N/A |
| Fair value adjustments | 8.2 | | (157.1) | 153.1 | N/A | N/A |
| Natural gas margins | 61.7 | | 107.8 | 101.4 | (42.8)% | 6.3% |
| | | | | | | |
| Operating and maintenance expense | 117.6 | | 188.6 | 181.2 | (37.6)% | 4.1% |
| Impairment losses on property, plant, and equipment | 43.2 | | 0.7 | 0.5 | 6,071.4% | 40.0% |
| Restructuring expense | 8.3 | | | | | |