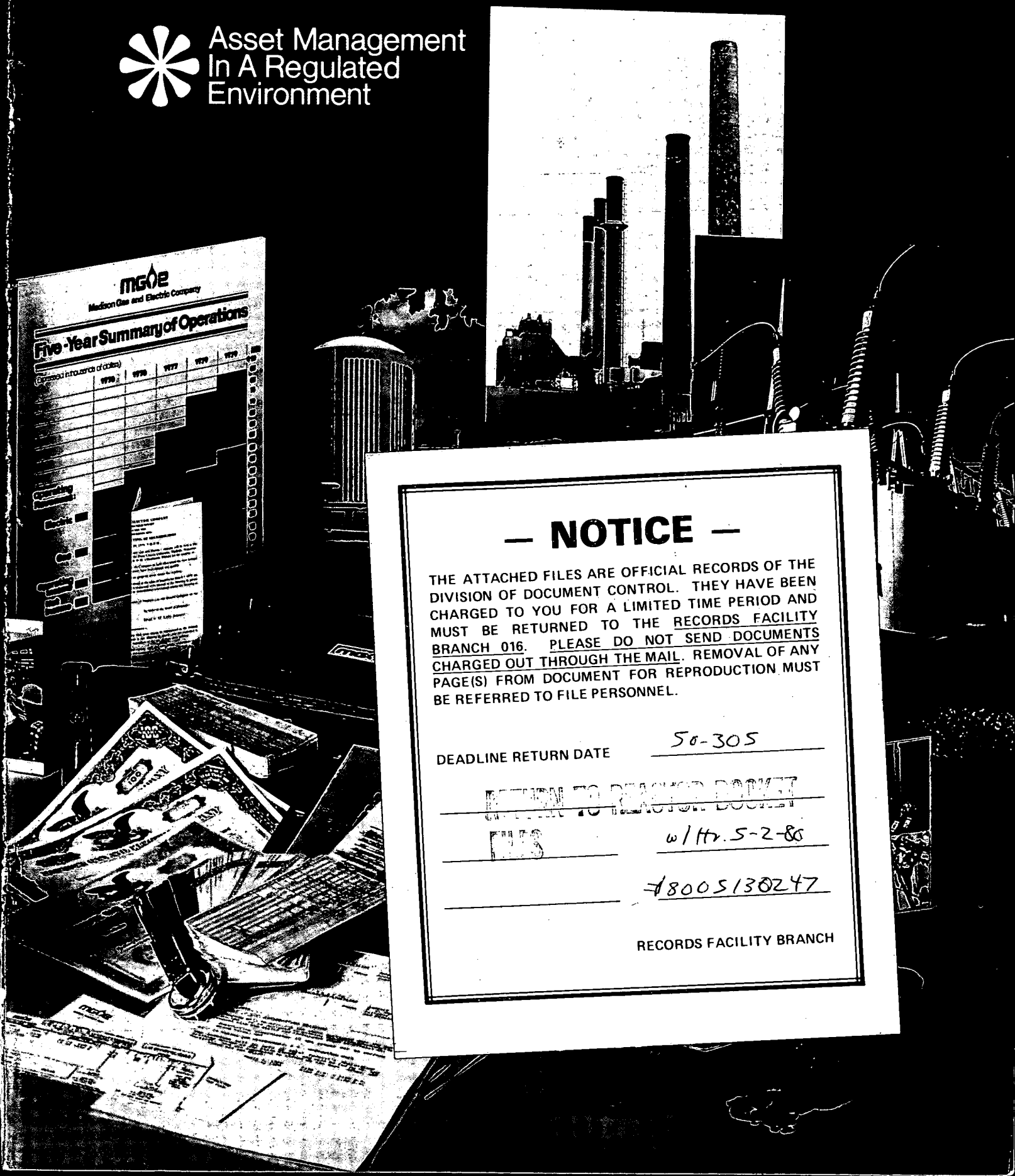
Madison Gas and Electric Company 1979 Annual Report

Asset Management In A Regulated Environment



Officers

William A. McNamara
Chairman of the Board
Age 71, Years of Service, 21

Donald J. Helfrecht
President and General Manager
Age 58, Years of Service, 33

Leo E. Brodzeller
Executive Vice President
Age 62, Years of Service, 40

Gerald A. Wilson
Group Vice President-Energy Supply
Age 57, Years of Service, 13

Frank C. Vondrasek
Vice President-
Electric System Operation
Age 51, Years of Service, 9

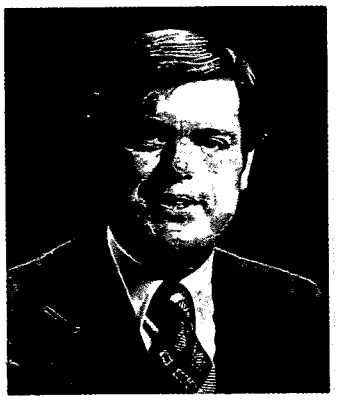
Richard M. Lawrence
Vice President-Community Affairs
Age 53, Years of Service, 29

Dale W. St. John
Secretary and Assistant Treasurer
Age 55, Years of Service, 15

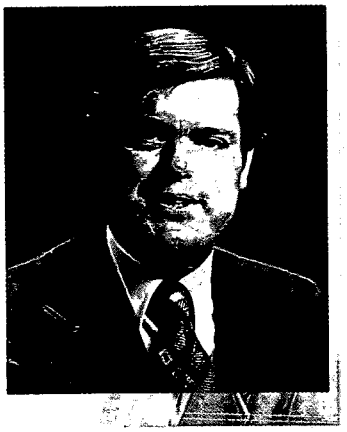
G. Howard Phipps
Treasurer and Assistant Secretary
Age 36, Years of Service, 7

B. C. Moore
Assistant Vice President and
Manager-Consumer Services
Age 58, Years of Service, 34

Terrence J. Schuh
Assistant Vice President and
Director of Rates
Age 37, Years of Service, 11



Beverly R. Duncan
Assistant Secretary-Corporate Affairs
Age 48, Years of Service, 29



Carol A. Bethke
Assistant Secretary-Administration
and Investor Relations
Age 40, Years of Service, 13

The Year At A Glance

	1979	1978	Percent increase (decrease) 1979-1978
Operating revenues	**$144,380,000**	$124,979,000	15.5%
Operating expenses	**$123,651,000**	$103,590,000	19.4
Net income	**$ 12,822,000**	$ 13,359,000	(4.0)
Earnings on common stock	**$ 9,628,000**	$ 10,558,000	(8.8)
Earnings per common share outstanding	**$1.76**	$1.96	(10.2)
Cash dividends paid per common share*	**$1.48**	$1.44	2.8
Weighted average number of shares outstanding	**5,477,541**	5,376,758	1.9
Book value – year end	**$17.76**	$17.54	1.3
Electric sales to consumers	**1,609,525 mwh**	1,599,502 mwh	0.6
Electric customers in service – year end	**95,237**	93,458	1.9
Average use per residential customer	**5,897 kwh**	6,241 kwh	(5.5)
Electric system one-hour net peak demand	**349,000 kw**	370,000 kw	(5.7)
Gas sales to consumers	**19,141,000 mcf**	17,780,000 mcf	7.7
Gas customers in service – year end	**63,466**	60,989	4.1
Gas system peak day	**129,776 mcf**	129,216 mcf	0.4
Investment in plant	**$346,236,000**	$330,387,000	4.8
Total capitalization (incl. interim loans)	**$235,226,000**	$233,461,000	0.8
Number of employees – year end	**549**	512	7.2

*On February 15, 1980, the directors authorized an increase of 4 cents per share in the quarterly dividend, payable March 15, 1980, increasing the total dividend to 41 cents per share quarterly or the equivalent of $1.64 per share annually.

Business Description

Madison Gas and Electric Company generates, transmits, and distributes electric power, and purchases and distributes natural gas in the Madison trading area. The electric service area covers about 220 square miles, and natural gas is distributed throughout a 750-square-milc area. While its service area is compact, it is a growing community with a population of about 250,000 in the Cities of Madison, Middleton, Monona, two adjoining villages, surrounding areas including ten outlying villages, and the Cities of Lodi and Verona.

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To Our Shareholders

The year 1979 saw a continuation of our efforts to maintain earnings and dividend levels in the face of increasing expenses due to rampantly escalating fuel costs, substantial inflation, and continuing mandated expenses in the interest of preserving the environment and increasing regulatory requirements that do not produce revenues.

Revenues and Expenses Increase

Total revenues were $144 million, an increase of 15 percent over 1978 revenues of $125 million. Operating expenses, however, were $124 million, an increase of 19 percent over 1978 expenses of $104 million. The fact that expenses rose faster than revenues underscores our need for rate relief.

Earnings in 1979 were $1.76 per share compared to $1.96 in 1978, a decrease of 10 percent. Total earnings of $9.6 million produced a 9.9 percent return on common stock equity, substantially less than the 13 percent return authorized by the Public Service Commission of Wisconsin (PSCW) in our last rate order issued in 1976.

Dividends Up

Dividends paid per common share totaled $1.48 in 1979, an increase of $.04 from the $1.44 paid in 1978. We have been able to maintain our long-term trend of increasing dividend payout, even though earnings per share have not increased at the same pace.

Rate Increases Requested

We filed an application for increases in electric and gas rates with the PSCW on May 31, 1979, the first since the general rate increase authorized in November, 1976. On February 14, 1980, the PSCW approved a $9 million annual electric and gas rate increase. The increase represents only 62 percent of the $14.5 million requested. The amount we asked for was based on estimates of 1979 revenue requirements that were made in late 1978. After filing the complete rate case in accord with the PSCW requirements, additional estimates based on 1980 needs were provided to the Commission Staff. In its final decision, the Commission adjusted the 1980 estimates, including an increase in the revenue totals at present rates. It also lowered the requested return on common stock equity, thereby reducing the amount of the increase.

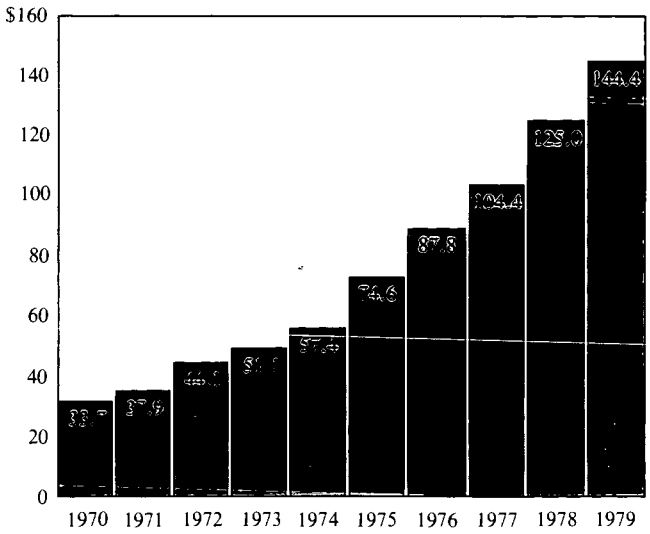
We had requested a 14 percent return on common stock equity. The PSCW order was based on the 13 percent return authorized since November, 1976, when the prime interest rate was 6.5 percent and the Consumer Price Index was rising about 9 percentage points annually. Reducing our request is an unenlightened step backwards in this period of high money costs and uncontrolled double-digit inflation, with no relief in sight.

From the time we first started to prepare our rate case to the time that the new rates were approved, the Consumer Price Index increased over 13 points. This increase in all prices adversely affects the Company's operating costs and further erodes the effect of the rate increase. The time period involved in securing rate increase approvals is a major factor to be considered by MGE when reviewing future revenue needs.

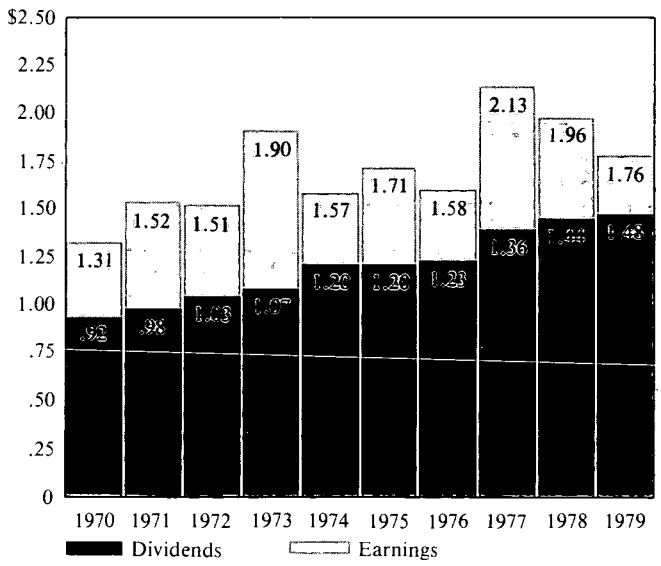
In 1978, we earned 11.3 percent on our common stock. The return on investment was 9.9 percent in 1979, a year in which the prime interest rate rose to over 15 percent. The effect of declining earnings is to reduce interest in our securities on the part of investors, who furnish the money to pay for needed equipment and facilities. The resulting need to pay more for capital will result in higher rates for utility service to all consumers.

The $9 million increase just authorized will result in approximately $6 million more in electric service revenues and $3 million more in gas service revenues. The average residential electric customer probably will pay about $18 more per year. Natural gas costs will increase about $21 per year for a typical residential space-heating customer.

Revenues (millions)



Dividends and Earnings (per common share)



Sales Increase

Our increases in sales of electricity in 1979 reflect significant sales of power to other utilities, in excess of $22 million. Forty percent of these sales occurred during the first three months of 1979, when severe cold weather restricted delivery of coal to utilities in other areas.

We added 1,779 new electric customers during 1979, continuing the steady growth trend in our customer base. We had a cooler-than-normal summer, which reduced the air-conditioning load so that a new summer peak was not reached for the first time in several years.

The number of gas space-heating customers increased by 2,858. Rising petroleum prices and concern about possible oil shortages spurred many customers to convert to gas in addition to the normal growth in customers we would expect from population increases. The new customers are mainly residential and small commercial users. Total gas sales increased 8 percent, to 193 million therms this year.

Generating Capacity Good

Our net summer electric generating capability is 597 megawatts, of which 15 percent is nuclear, 70 percent is coal, and 15 percent is combustion turbines. This capacity places us in the enviable position of not having to build additional plants in the near future. Through our pooling arrangements with two other Wisconsin utilities, we are a net seller of both capacity and energy. A study of our capacity made this year concludes that our situation produces good revenues and operates to the advantage of our customers and shareholders. We expect to remain in this selling position for several years.

Gas Supply Promising

Our sole supplier of natural gas is the Michigan Wisconsin Pipe Line Company. It is one of the leaders in the High Island Offshore System in the Gulf of Mexico, from which gas is now flowing. It is very active in developing supplies in the Rocky Mountain overthrust area and other western United States locations. The pipe line company continues to explore in Alabama, Mississippi, and offshore Texas and Louisiana. We believe it will be able to meet our gas requirements for many years, and we expect to be able to continue to accept new customers and provide them with clean, economical gas service.

Employees a Major Factor

A major asset of any organization is its people. The experience and knowledge of MGE employees in all areas are major factors in our ability to cope successfully with the many contrary forces that impinge on a regulated utility.

One-year agreements, effective May 1, 1979, were completed with the two unions representing our 126 clerical and 261 operating employees. Discussions regarding renewal of the agreements will begin in March, 1980.

Economy of Madison

The stable growth of the Madison area is an asset to the Company. The economy does not rise or fall to the extent that we see at state or national levels. It is somewhat recession proof. The strongest overall measure of its stablity is employment; at the end of 1979, unemployment was 3.6 percent in the Madison area compared to 4.7 percent for the state of Wisconsin and a seasonally adjusted rate of 5.9 percent for the country. This stability is a result of the high proportion of the population that is employed in government, by the University of Wisconsin, and in closely associated research-oriented companies or institutions.

We appreciate your support, confidence, and interest in Company affairs. We look forward to providing continuing good service at a reasonable cost and, at the same time, maintaining an adequate return on your investment.

For the Board of Directors

William A. McNamara
Chairman of the Board

Donald J. Helfrecht
President

D.J. Helfrecht (left) and W.A. McNamara (right).

Electric Operations

The mission of any business is to manage the assets provided by its owners in their best economic and social interests, as well as those of its customers, employees, and the public at large. For a heavily regulated company—such as a utility—this has always meant providing energy on an instantly available, extremely reliable basis at a return on investment sufficient to minimize the cost of capital necessary to finance the effort. In today's increasingly regulated environment, utilities are ordered to discourage the use of the product they have to sell, while incurring mandated new costs in the interests of protecting the environment and providing economic relief to the disadvantaged. What follows presents the traditional report to shareholders in terms of the challenge to manage the assets of an electric and gas utility in an increasingly regulated environment.

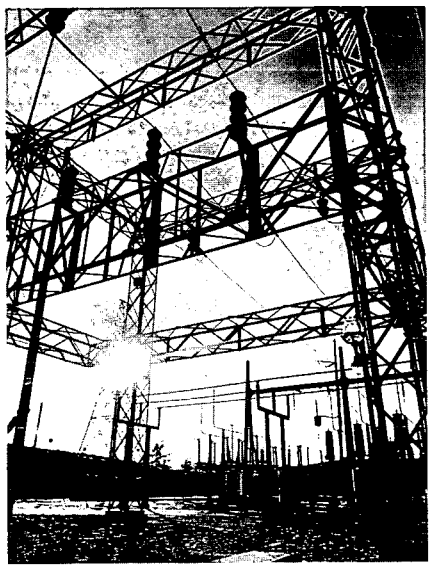
Electric Operations

Madison Gas and Electric currently serves more than 95,000 customers with electricity in a 220-square-mile service territory, compared with 75,000 customers a decade ago. Revenues rose from $19.7 million in 1970 to $89.2 million in 1979, while electric sales have grown from 1.3 billion kilowatt-hours (kwh) to 2.3 billion kwh; these figures include sales to other utilities.

Generating Capacity Adequate

With the completion of the second 527-megawatt (mw) unit at the Columbia Energy Center (Columbia) near Portage, Wisconsin, in 1978, MGE's total net generating capacity grew to 597 mw. Coal-fired generation is 70 percent of the total net summer capacity, counting the Company's share of both Columbia units and several smaller units at its Blount Station in Madison. The rest of its generating capacity is 15 percent nuclear (MGE's 93-mw share of the Kewaunee Nuclear Plant) and 15 percent combustion turbines.

MGE's long-term generation capacity plans include refurbishing existing units at Blount to extend their useful life beginning in 1987, and the possible addition of new capacity at Blount later on. Participation planned with other eastern Wisconsin utilities in additional jointly owned generating units in the mid-'90s would add approximately 200 mw of capacity then.



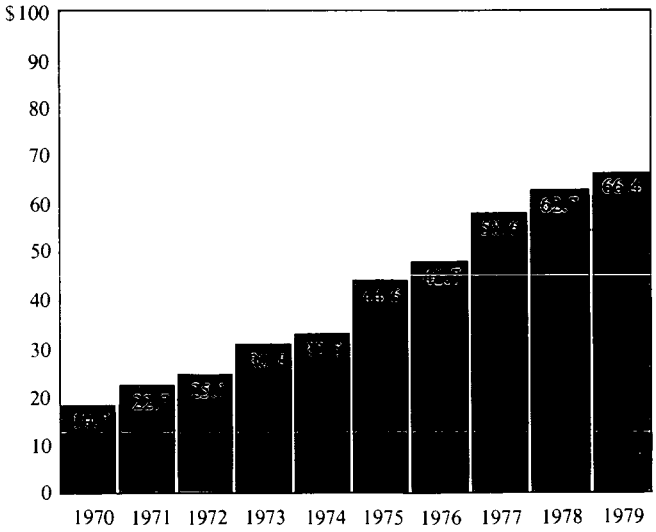
138-kv switchyard and equipment at MGE's Fitchburg substation.

Generating Reserves Good

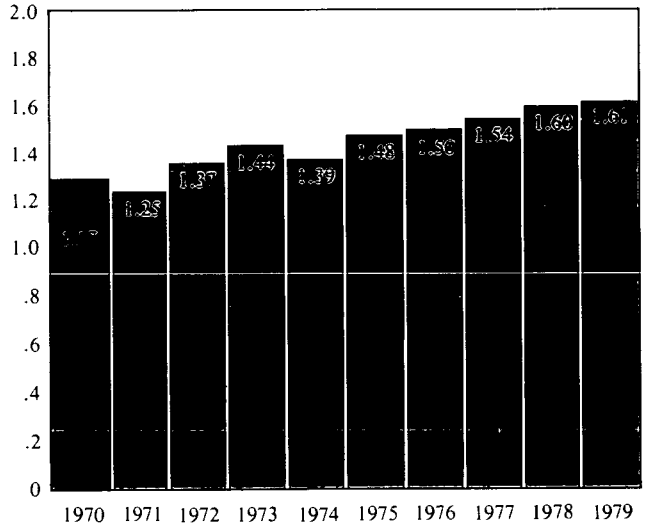
Through the generating capacity pooling arrangements with the two other members of the Wisconsin Power Pool—Wisconsin Power and Light Company and Wisconsin Public Service Corporation—generating reserves for all three companies are equalized. That is, each utility's reserve capacity is placed into the pool and then allocated back to each on the basis of the peak demand on each company's system. Under this arrangement, MGE currently is a net seller of both capacity (kilowatts) and energy (kilowatt-hours).

Booz, Allen & Hamilton, an independent consulting firm, was retained by the Company last year to review the Company's capacity utilization and sales to other utilities. Their findings show that MGE's capacity is being utilized effectively. The study also shows that revenues from sales of capacity and energy adequately compensate MGE for the costs involved and benefit both customers and investors. It also points out that customers enjoy lower rates as a result of MGE's

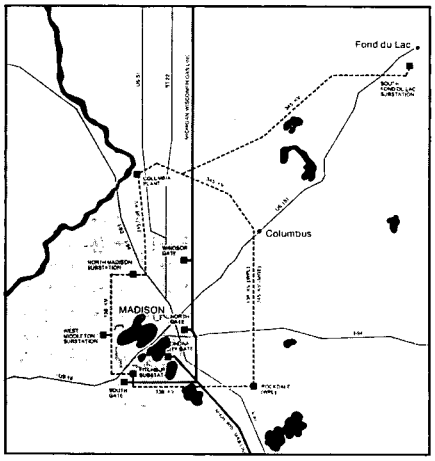
Revenues (millions) (retail)



Sales — kwh (billions) (retail)



past planning decisions to provide generating capability during less inflationary times.



Location of major electric and gas facilities.

Fuel Mix Varied

During 1979, the Kewaunee Nuclear Plant provided 26 percent of total net generation, and the Columbia Energy Center furnished 47 percent. The remaining 27 percent was furnished by the Blount Station and the combustion turbines located in the Madison area.

During 1979, energy sales to other utilities were 30 percent of MGE's total net generation. The bulk of these sales occurred during the first quarter of the year when severe cold weather restricted coal supplies east of Wisconsin, creating need for utilities there to import power. As a result, sales to other utilities were more than twice what MGE could have reasonably expected on the basis of normal, predictable demand.

Refuse-derived Fuel Project Progressing

The joint project of the City of Madison and MGE to use residential refuse for fuel to generate electricity is near completion. One boiler at Blount Station has already been converted to burn the refuse-derived fuel (RDF) along with coal and is in service. Conversion and testing are underway on the second boiler to be included in the project. The City is operating and adjusting the equipment at its refuse-processing facility that provides a reliable supply of combustible material from the refuse it collects.

The two boilers modified at Blount will burn about 120 tons of refuse per week, potentially saving 15,000 tons of coal (about 7 percent of the amount used at Blount). RDF will represent about 2 percent of MGE's total fuel mix.

This cooperative project will recover energy from a previously discarded resource and further save money by reducing requirements for increasingly costly landfill sites. The cost of the refuse-receiving facility and boiler modifications at Blount Station was borne by the City. MGE reimburses the City for the refuse used based on its value as a fuel.

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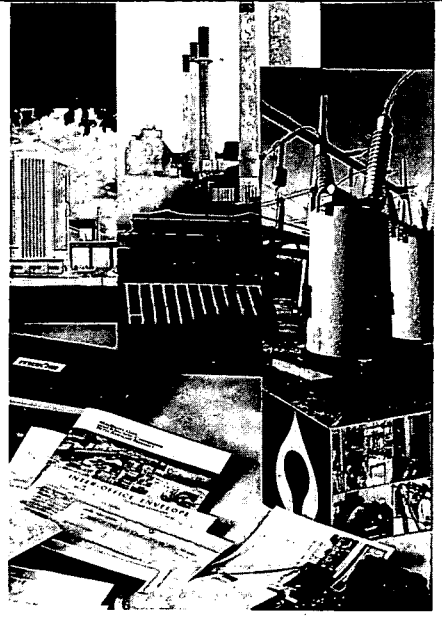
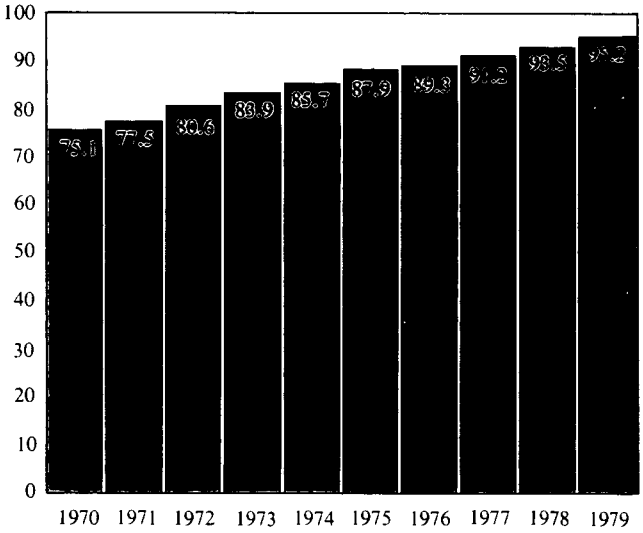
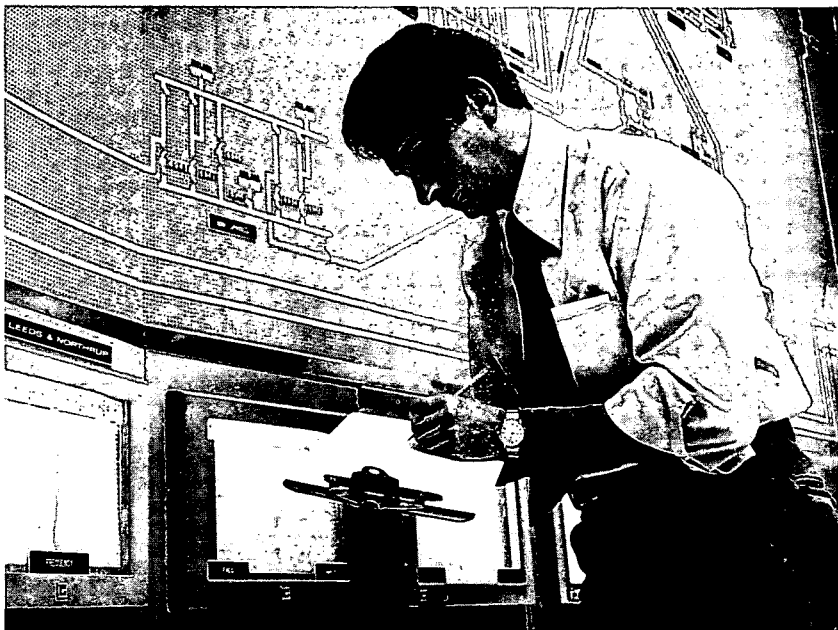


Number of Customers (thousands)





Assistant Supervisor—System Operations R. Feller monitoring power supply recorders.

Electric Operations

69-kv Line Under Construction

Work on a 7.5-mile, 69-kv line connecting the Walnut and West Middleton substations started in 1979. This project will be finished and placed in operation in 1980.

In the fall of 1978, the PSCW first authorized MGE to construct a 3.2-mile segment of the line overhead through Madison and Middleton, but opposition from the City of Madison and nearby residents prevented construction. The City would not grant a conditional use permit required by a zoning ordinance to allow construction of the overhead portion. The Company appealed this matter to the PSCW and to the courts.

In February, 1979, the PSCW reversed its earlier authorization, and ordered MGE to construct the 3.2-mile segment underground. Undergrounding this segment will add about $1.8 million to the cost, increasing the total cost to $3.2 million.

The line makes capacity available from the 138-kv transmission supply west of Middleton to the near west side of Madison. Load growth is substantial here, especially with the completion of the University of Wisconsin's Clinical Science Center in March, 1979. The $105-million Center contains 1.5 million square feet of usable area, including a 549-bed hospital. This new line is critical to continuity of electric power supply to the new University medical complex.

Transmission Route Dispnted

Early in 1979, the PSCW authorized construction of one of two 138-kv electric transmission lines MGE had proposed in the summer of 1976. The 13.5-mile-long approved line will connect North Madison substation, near DeForest, to Sycamore substation on Madison's east side and will follow Interstate 90–94.

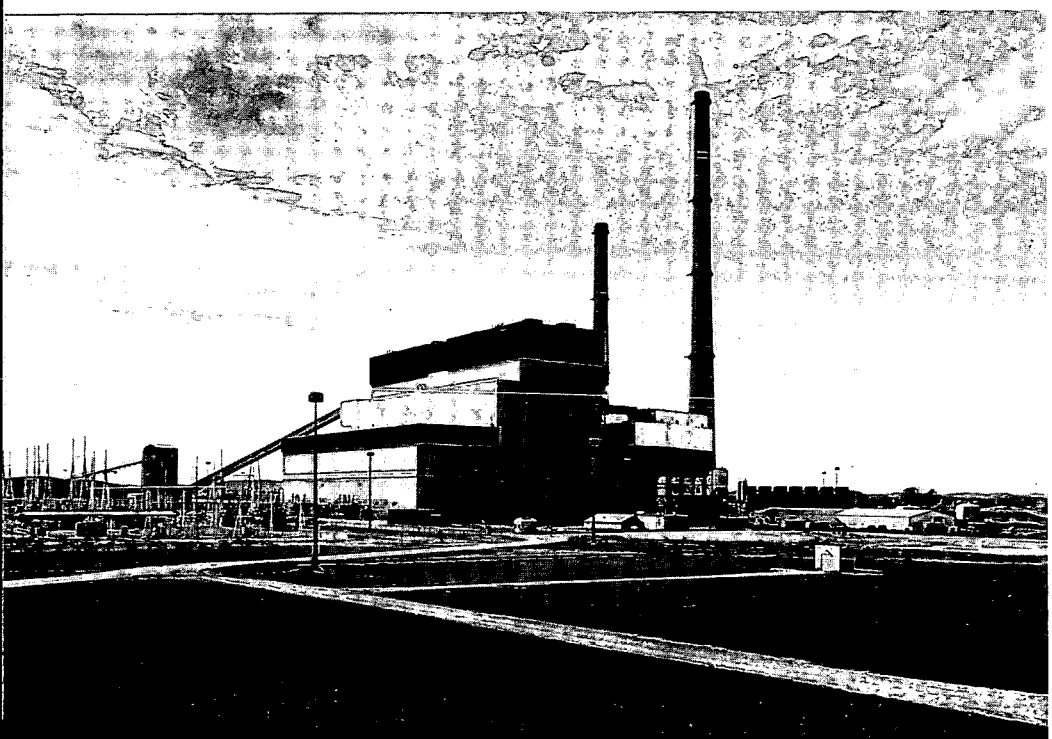
The PSCW environmental review staff rejected the other 138-kv transmission line that was proposed to run along fence and property lines through open farmland directly south from North Madison substation to Huiskamp substation in the town of Westport. The Commission ruled that a 138-kv line between Sycamore substation and Blount Station be substituted for the North Madison to Huiskamp line and that it should be underground between Blount and Highway 30. An existing overhead 69-kv line located here will also be placed underground as a result of this ruling.

Second Advance Plan Submitted

Planning for future electric generation, transmission, and distribution facilities once was relatively simple. Before the mid-'60s, future loads were readily predictable based on historical trends. New facilities to meet increasing loads were generally added on an individual utility basis. Generating units generally were constructed at a lower cost per unit of capacity than previous ones due to economics of scale and improving technology.

The factors influencing planning have grown more complex, requiring coordinating efforts between neighboring utilities. Responding to this increased complexity in systems planning, MGE joined some years ago with three other Wisconsin power companies and one Upper Peninsula (Michigan) power company to form the Wisconsin–Upper Michigan Systems (WUMS). This group promotes coordination of planning, design, construction, and operation of generation and transmission facilities to achieve maximum reliability and economy of service in the areas served by the WUMS companies.

The Eastern Wisconsin Utilities (EWU), made up of the three other Wisconsin WUMS companies and MGE, is a subgroup of WUMS and files a combined Advance Plan with the PSCW on a biennial basis as a result of the Wisconsin Power Plant Siting Act of 1975. This joint plan includes a detailed review of the demand and energy forecasts of the individual EWU companies. Also included are detailed reviews of the EWU future generation requirements, additional bulk transmission requirements, and



Columbia Energy Center, near Portage, Wisconsin, is owned jointly by MGE, Wisconsin Power and Light, and Wisconsin Public Service Corporation.

generating reserve requirements. This Advance Plan also reviews the individual EWU company conservation programs and research efforts in new technologies associated with generating, transmitting, distributing, and usage of electricity. The first Advance Plan by EWU was filed in 1976. The second Advance Plan was filed in March of 1979.

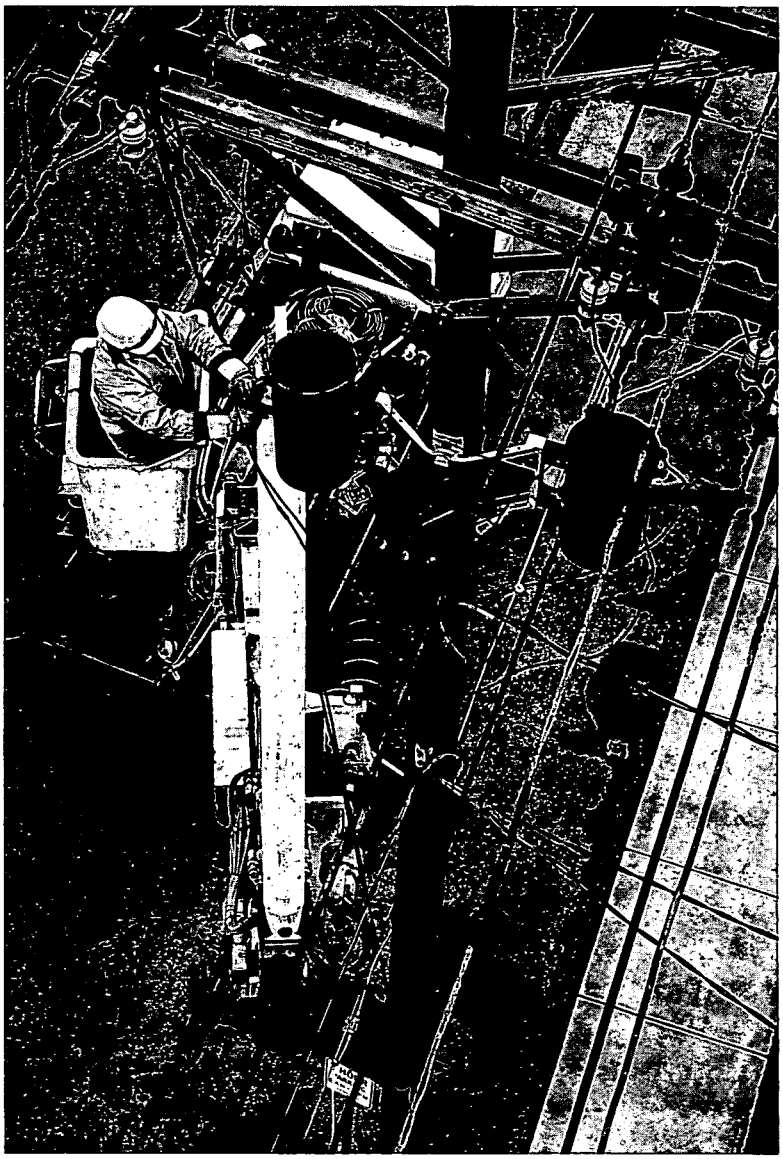
The MGE demand and energy forecast as filed in the 1978 Advance Plan predicts slightly smaller load growth than the Advance Plan filed in 1976. The long-term peak demand for electrical service now is expected to grow 3.25 percent per year, to a total of 766 mw by the summer of the year 2000, down from the earlier estimate of 3.41 percent.

Corresponding energy use by MGE customers is expected to increase at a long-term annual rate of approximately 3.17 percent, to over 3.5 billion kilowatt-hours (kwh) annual energy usage in the year 2000. This new projection is down from the 1976 projection of 4.07 percent. The actual energy used by MGE customers in 1979 was 1.6 billion kwh.

The rates of load growth are decreasing due to conservation and more efficient use of energy by MGE customers because of higher energy costs. Overall demand for electrical energy, however, is growing because of population growth in the MGE service territory and the corresponding commercial, educational, and industrial loads associated with these increases in population. It is predicted that over the next 20 years, the MGE service area will still experience its peak in summer due to new customers and growing air-conditioning loads.

Natural gas supplies are predicted to diminish starting around 1990. The reduced availability of natural gas for space heating will result in a faster growth rate in winter demands for electricity. This may cause MGE to again become a winter peaking utility.

Presently available and planned assets comprising the electric system are sufficient to serve the foreseeable needs of the service area economically, reliably, efficiently, and with reasonable reserves.



Line work progresses on an overhead distribution pole.

Gas Operations

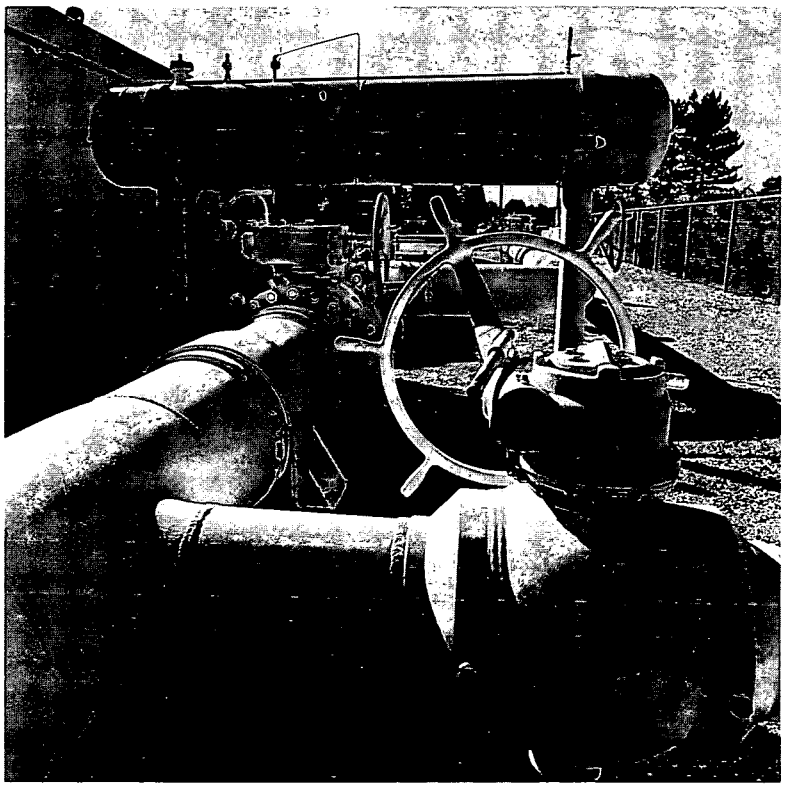
MGE has added about 1,900 new residential and small commercial natural gas customers per year over the past decade. The total number of gas users has increased from 45,000 in 1970 to more than 63,000 in 1979, located in a 750-square-mile service territory. Gas sales rose from 129 million therms in 1970 to 193 million therms in 1979, with revenues rising correspondingly from $12.5 million to $55.2 million.

Supply Outlook Good

The Michigan Wisconsin Pipe Line Company (Michigan Wisconsin), the supplier of natural gas to the Company for the past 30 years, aggressively continues efforts to develop new supplies.

Michigan Wisconsin obtains natural gas in the Texas-Oklahoma Panhandle area, the Louisiana offshore area, and others. It is a lead participant in developing the High Island Offshore System in the Gulf of Mexico, from which gas currently is flowing. It is actively working, also, to develop the Rocky Mountain overthrust area. Recent changes cutting the pipeline construction needed in the Wyoming Interstate Natural Gas System project will reduce investment in the project significantly and still bring this gas onstream through interchange agreements using other pipelines. Michigan Wisconsin obtains about 15 percent of its gas from Canadian sources and continues to explore in Alabama, Mississippi, and offshore Texas and Louisiana.

Michigan Wisconsin should be able to meet MGE's gas requirements under a contract extending to 1992, although it makes firm commitments only for each succeeding year. MGE's 1979–80 authorization will remain the same as in the previous year, 22.5 million mcf.

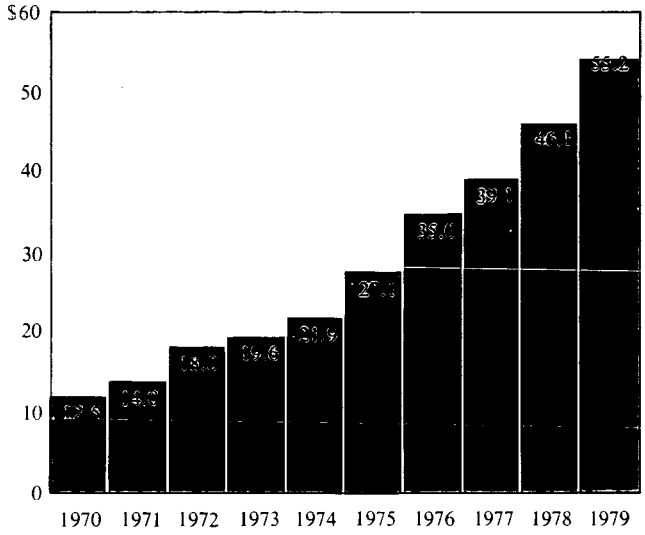


Piping at MGE's natural gas receiving station located on Femrite Drive.

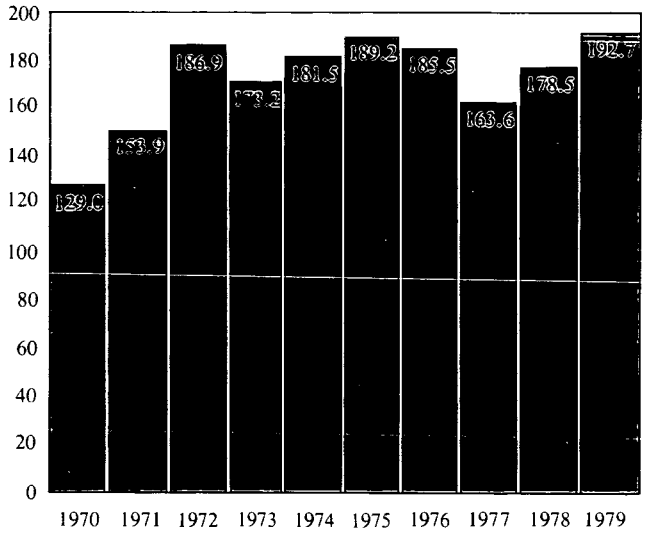
Roxbury-Dane Tie-in Completed

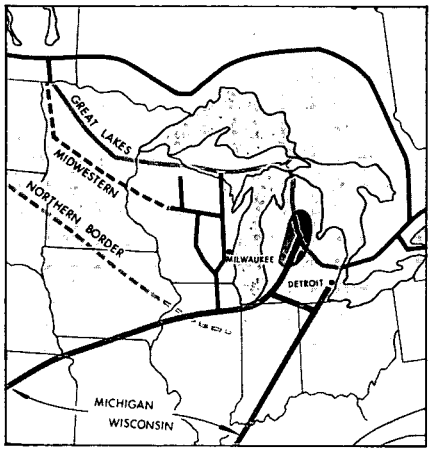
Construction of an 11-mile tie between two radial arms of the natural gas distribution system was completed in the Spring of 1979. This 6-inch-diameter gas line loops the western portions of the system in Dane county near the Village of Dane with existing facilities that end in the Village of Roxbury.

Revenues (millions)



Sales – therms (millions)





Natural gas pipelines that serve portions of the states of Michigan and Wisconsin.

This project reinforces the western part of the gas system where considerable customer growth is occurring, permits stabilizing gas pressure during peak use in winter, and makes service available to potential new customers.

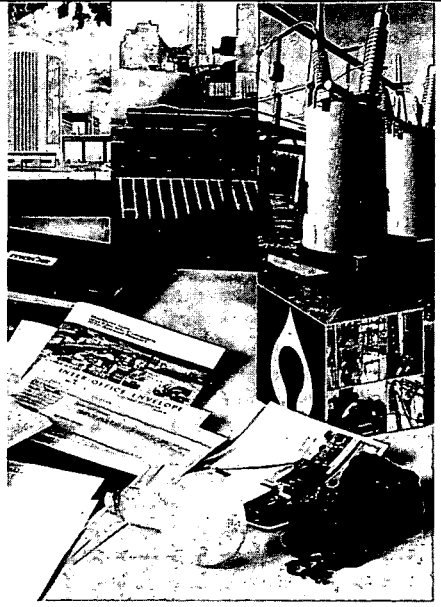
Gas System Expansion and Replacement Continues

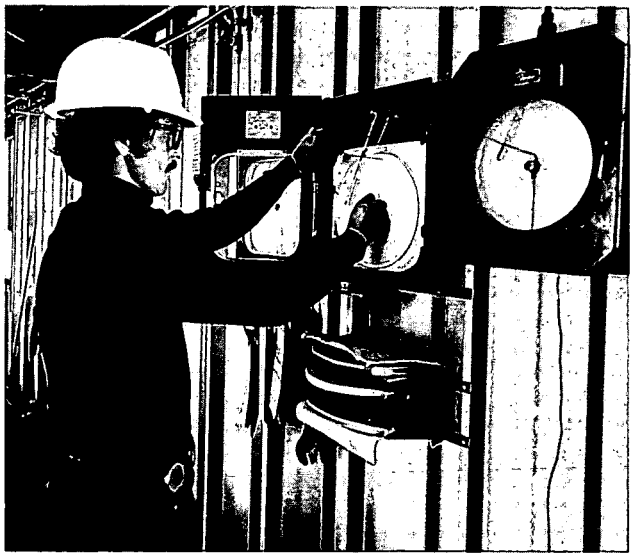
During 1979, nearly 2,500 new gas customers were added to the system, and conversions to gas space heating totaled about 2,900 this year. This demand for gas service reflects the sharp increase in heating oil prices and public confidence in gas as a clean, efficient, and available fuel.

A project to replace old, bare steel and cast-iron gas mains to meet federal and state safety code requirements moved at a quicker pace in 1979. Bare steel gas main replacement was completed last year, with replacement of the cast-iron mains scheduled for completion in 1983.

Some 25 miles of new gas main was added in 1979, roughly the same as the previous year. Gas main replacement totaled 26 miles, nine more miles than in 1978.

MGE has sufficient assets in place and available to serve future additional gas customers, both those who are converting and those to be added through new construction. The Company plans to continue its program of gas system replacements and upgrading to permit operation at the safest, most efficient levels possible.

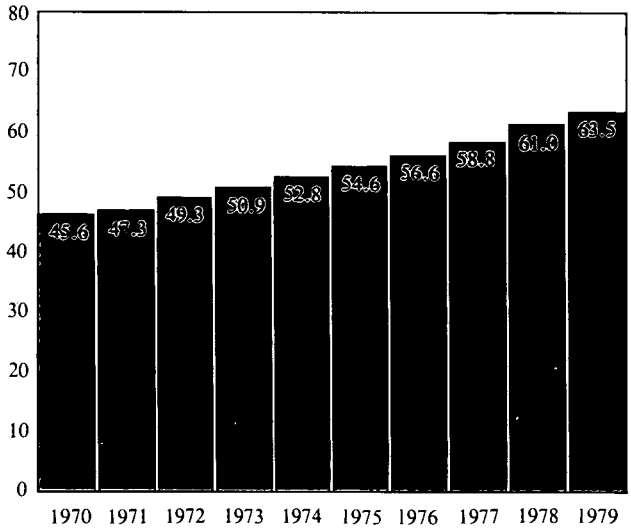




Gas Production Department Repairman R. Gorsuch changes recorder charts at an MGE Company gas receiving station.

Gas Distribution crew installs a section of 12-inch-diameter gas main.

Number of Customers (thousands)



Human Assets

One of the most valued assets MGE has is its 549 full-time employees. The Company is committed to developing an atmosphere that fosters growth and career development for all employees. Advancement from within has always been a Company practice.

The number of employees increased 7 percent during 1979. In many cases, these new employees were recruited to add skills in specialized areas—such as data processing, rate analysis, engineering, records management, and energy utilization. Such additional technical expertise is required because of the increasingly greater complexity and sophistication required in design, construction, and operation of all utilities today. Staff increases in recent years also reflect the need to respond efficiently and promptly to the ever-increasing regulatory demands posed by local, state, and federal authorities.

New labor contracts negotiated between MGE and its two bargaining units—the International Brotherhood of Electrical Workers, Local No. 2304, and the Office and Professional Employees International Union, Local No. 39—became effective May 1, 1979. These one-year agreements, covering some 126 clerical and 261 operating employees, conform to federal wage and price guidelines.

Employee Training Upgraded

Realizing the growing importance of preserving positive relations between customers and employees, the Company expanded its customer relations training program this year. In 1979, some 160 employees participated in a course aimed at improving the interpersonal communication abilities of those people in customer-contact positions. The course also increases employee motivation and aids in problem solving. In 1978, about 100 employees received this training.

Work Dispatcher R. Elert (at computer terminal) and Office Service Representative J. Richgels (at radio) work in dispatcher's office.

A managerial/supervisory training course dealing with job instruction and delegation principles was tested late in 1979; it is scheduled for full implementation beginning early in 1980.

Major changes in the Company's Tuition Reimbursement Program were made in 1979 to help offset spiraling education costs. Benefits were increased to include 80 percent reimbursement of registration, tuition, laboratory fees, and text costs for approved courses at a variety of educational institutions. This program, begun in 1965, provides incentive and financial assistance for employees to better qualify themselves for current and future work with the Company.

Information Systems Expauding

The decade of the '70s was a volatile period for the utility industry. Rising fuel and capital costs, coupled with increased federal and state regulation, resulted in mounting pressure on management for timely, detailed information—a prime requisite for intelligent decision-making and strategic planning. The Company's Data Processing Department took on an increasingly vital role in data collection and analysis.

Recognizing the potential for a substantial return from sound investments in computer-based information, the Company named a steering committee in 1979 to help design and coordinate an effective plan for using the Company's data processing resources. This group promotes sound planning to improve the quality and timeliness of information needed. The committee is developing a five- to ten-year strategic information systems development plan that will outline computer applications for cost savings, better customer service, and improved operational effectiveness.

Consultants specializing in utility information systems have been hired to analyze the Company's information needs; their findings will focus on ways to lower costs through a more effective and efficient use of human resources, to improve coordination between computer-using departments, and to integrate manual and automated systems.

Data Processing Supervisor J. Stone works at cathode ray tube computer access terminal.

In a related area, the automated word processing system, which has greatly increased productivity in the handling and production of written material (and which currently includes one on-line application), is being considered for possible further computer applications to increase the benefits already being realized by utilization of this automated equipment.

Conservation Communications Increases

In response to increasing demand for practical energy conservation information, MGE has intensified its efforts to inform its customers through various media and employee contacts.

The Consumer Services staff completed over 3,600 free home insulation and weatherization audits last year, 400 more than in 1978. This brings the total number of inspections completed to 10,250 since the program started in September, 1976. The Consumer Services Division logged 20,000 telephone, mail, and in-person contacts with MGE customers—dou-

Supervisory Assistant—Energy Utilization Department J. Stellner points out insulation features shown in an MGE display.

the 1978 total—to further advance the conservation ethic.

Some 19,000 Company-produced energy conservation brochures and pamphlets—covering topics from cooling to lighting to insulating to weatherizing—were distributed upon requests from customers during 1979. A six-page MGE newsletter dealing with efficient and safe use of natural gas and electricity is mailed to customers with their monthly statements.

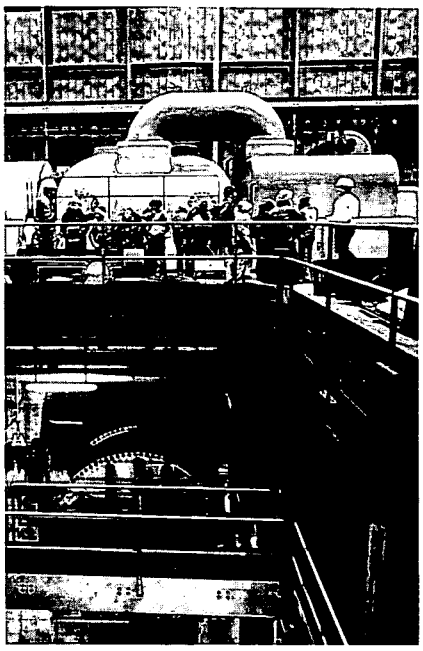
Some 200 energy conservation and education presentations were made by MGE employees to school, church, civic, and service groups during 1979, nearly twice as many as given the year before.

A series of five new television commercials was produced to broaden the base of the MGE conservation information program. Studies show that MGE's use of television has been highly effective in increasing public awareness of the energy and dollar savings that can be realized by implementing good conservation habits. An MGE electrical safety program for consumers, using television and print media, is being developed for the summer of 1980.

Cooperative Efforts Initiated

The Company actively collaborates in energy conservation projects with government agencies and utility industry associations on the local, state, and national levels. MGE also is involved in local safety and alternative energy programs. A grant made last year by MGE to Operation Fresh Start, Inc., a nonprofit rehabilitation and employment training program, was approved to provide solar domestic hot-water collectors and other equipment for two single-family homes being converted into passive solar homes. Information collected on the performance of these solar installations will be used to analyze their effectiveness in the Company's service area.

The Company also participated in a program with the City of Madison to alert the public in the Madison area to the hazards of hot tap water scalds. This project utilized radio and print to acquaint people with the potential dangers.



A student group touring the Blount Station next to a turbine generator.

Shareholders' Profile

The owners of the Company are located, for the most part, in or near the MGE service area. Some 56 percent of the 17,711 registered shareholders are in Wisconsin—about 3,000 in the Company's service area. An additional 15 percent live in the adjoining states of Illinois, Iowa, Minnesota, and Michigan. The remaining 29 percent are distributed throughout the rest of the United States.

Distribution of ownership shows that 23 percent have less than 100 shares, 67 percent of the holders own between 100 and 500 shares, and 10 percent own more than 500 shares.

Annual Meeting Innovation

The 1979 annual meeting of shareholders was held in the evening for the first time with the objective of stimulating greater attendance. Over 250 persons attended—several times more than the number present at the usual afternoon meetings of the past. Among this larger group were a number of employee shareholders who had been unable to attend the previous meetings held during daytime hours.

The 1980 annual meeting is scheduled to be held Thursday, April 17, 1980, at 7:30 p.m., at the Holiday Inn Southeast, located at the Interstate 90-94 and U.S. Highway 12-18 interchange.

Attendees at 1979 annual shareholders meeting view exhibits.

The Role of Rogulation

A fact of life that is continuing to increase its impact on everyone is government. This is especially true for utilities—regulated monopolies by design for generations. During 1979 MGE experienced greater regulatory impact than ever before from all levels of government. Such regulation affects MGE's ability to serve its customers efficiently and to do so in a manner that also protects the integrity of the shareholders' investment. In many instances, the impact of more than one segment of government is felt in the same area. Such impacts often work at cross purposes as some authorities mandate increased expenditures, while others press for keeping rates down. As desirable as a clean environment may be, the costs the Company incurs are paid for by its customers in the end.

Treasurer and Assistant Secretary Phipps testifies at 1979 rate hearings with Hearing Examiner J. Wolter presiding.

Blount Station Stack Emissions Questioned

The northeast side of Madison has been declared by the U.S. Environmental Protection Agency (EPA) to be a nonattainment area for meeting air quality standards with respect to sulfur dioxide (SO_2) concentrations. MGE's Blount Station is considered to be a possible contributor to this air quality problem.

The Wisconsin Department of Natural Resources (DNR) has issued rules that will limit the Blount Station's SO_2 emissions if the DNR finds the station to be contributing to the nonattainment condition.

If the DNR says that Blount Station must reduce its emissions, the most practical method would be for MGE to utilize Midwest low-sulfur coal. Using this low-sulfur coal, however, could increase costs (and also rates) an estimated $1.2 million to $1.8 million per year.

Ordinance Affects Transmission Lines

In a different situation, a previously unused part of the Madison zoning ordinances was involved in the decision made by the PSCW regarding the routing and undergrounding of a portion of the Walnut to West Middleton 69-kv transmission line. As mentioned on page 8, the change to underground installation and a slightly longer route added $1.8 million to the project, which ultimately will be paid for by customers. Besides the PSCW and City of Madison participation in this decision, the City of Middleton and a grass-roots neighborhood group also were involved in this matter.

Another transmission line project complicated by regulatory authority is a 138-kv line on Madison's east side. Compliance with the same zoning ordinance is required. Although the PSCW has approved a route following that of an existing 69-kv line and stipulated that both the existing and new lines be put underground, several years will pass before final City approval is obtained. Study of the various aspects of this project is just starting, so it is not possible now to estimate the cost impact that the delay will have.

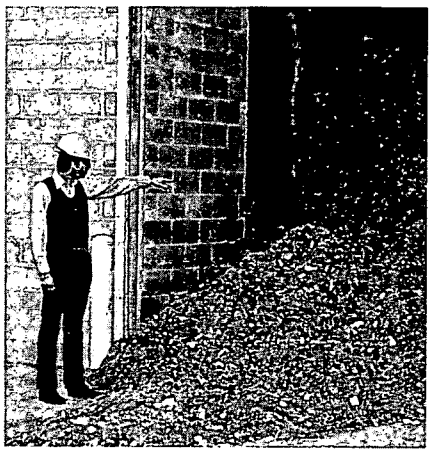
Energy Conservation

In the realm of energy conservation, a surplus of regulation is available to guide utilities. In 1979, the PSCW issued orders mandating energy conservation construction standards to be met before existing homes can receive gas space-heating service. This

Electrostatic precipitator for No. 7 boiler at Blount Station.

Crew installs underground piping that will contain 69-kv electric cable and cooling oil.

regulation requires large utilities to perform an energy audit or inspection to determine where a house may be deficient. The federal Department of Energy Residential Conservation Service rules that become effective December 1, 1980, duplicate these efforts with minor differences. In addition, the Wisconsin Legislature began considering proposals early in 1980 that would cover the same areas over which the federal law and PSCW rules already have jurisdiction.



P. Casey, Plant Engineer—Electric Production, with processed refuse ready for use in Blount Station boilers.

Disconnectiou Moratorinm Set

Again this winter, the PSCW ordered a moratorium on disconnection of residential service for nonpayment of bills. Disconnections are not permitted if a possible hazard to health could result from loss of utility service. Disconnection of commercial service is allowed if no residential living units are involved. The Company has a history of exercising responsible discretion concerning disconnections, especially those cases that could result in injury to health or damage to property. A number of financially able MGE customers appear to be abusing the PSCW order by refusing to pay their bills promptly—placing a burden on customers who do pay on a current basis.

Bad debts have increased substantially over the last several years due to these moratoriums. The Company uses every available legal remedy to collect from customers who refuse to pay their bills, including evening and weekend contacts, and Small Claims Court action during periods when disconnections are not permitted. In 1979, $190,000 was written off as uncollectible, an amount almost three times higher than the $67,000 written off in 1974, the year before the first moratorium. These write-offs will, of course, be covered ultimately by financially responsible customers.

Besides offering customers with delinquent accounts both deferred payment and budget billing plans, MGE also cooperates closely with social service agencies that provide financial support to the needy. During the past year, several government programs provided funds to low-income and elderly customers for heating bills.

Overall Effect Great

None of this reporting should be considered to be criticism of programs for reducing air pollution, of undergrounding transmission facilities, or of increasing energy conservation. They are merely specific examples of government's effect on the Company's operations. In addition, MGE, like other businesses, must comply

with the myriad regulations imposed by such other groups as the Occupational Safety & Health Agency, the Equal Employment Opportunities Commission, the Federal Energy Regulatory Commission, the Department of Energy, the Securities and Exchange Commission, and others. When the regulatory/legislative forces that currently prevail are considered together, they impose substantial impact on the Company. The most obvious impact is the direct cost involved in compliance that does nothing to bring in revenue. Less apparent is the need for more employees and more time to perform required studies, prepare reports, accumulate data for use by staffs, etc.—which also adds substantially to cost. The effect of these increased costs is to increase the need for additional revenues to cover them.

Superintendent—Energy Utilization R. Kokette measures window during energy conservation audit.

Summary of Operations

(Thousands of dollars except per share and shareholder figures)

	1979	1978	1977	1976	1975	1974
Operating Revenues:						
Electric	**$ 89,211**	$ 78,588	$ 65,256	$52,817	$47,407	$35,539
Gas	**55,169**	46,390	39,140	34,964	27,153	21,886
	144,380	124,978	104,396	87,781	74,560	57,425
Operating Expenses:						
Fuel used for electric generation and purchased power	**32,527**	24,377	17,321	13,766	12,787	13,491
Natural gas purchased for resale	**39,702**	31,480	25,525	22,720	16,651	11,769
Other operations and maintenance	**20,256**	17,310	15,004	12,837	11,236	9,753
Straight-line depreciation and amortization	**11,629**	10,496	9,215	8,496	7,378	5,455
Additional depreciation (equivalent to estimated reduction in income taxes)	**3,769**	4,832	2,741	3,345	3,059	2,658
Federal and state income taxes, including investment tax credit deferred—net	**10,347**	9,172	9,684	5,054	4,331	(81)
Property, payroll, and other taxes	**5,422**	5,923	5,131	4,607	4,037	3,567
	123,652	103,590	84,621	70,825	59,479	46,612
Net Operating Income	**20,728**	21,388	19,775	16,956	15,081	10,813
Other income and deductions—net	**300**	276	681	639	964	3,057
	21,028	21,664	20,456	17,595	16,045	13,870
Interest expense—net	**8,206**	8,305	7,685	8,939	8,041	7,412
Net Income	**12,822**	13,359	12,771	8,656	8,004	6,458
Preferred stock cash dividend requirements	**3,194**	2,801	2,613	2,635	2,252	1,445
Earnings on Common Stock	**$ 9,628**	$ 10,558	$ 10,158	$ 6,021	$ 5,752	$ 5,013
Earnings Per Average Common Share	**$1.76**	$1.96	$2.13	$1.58	$1.71	$1.57
Cash Dividends Paid Per Common Share	**$1.48**	$1.44	$1.36	$1.23	$1.20	$1.20
Operating Income Before Income Tax Items:						
Electric	**$ 28,182**	$ 28,605	$ 26,255	$19,690	$18,040	$ 8,885
Gas	**$ 6,662**	$ 6,787	$ 5,945	$ 5,665	$ 4,431	$ 4,505
Number of Shareholders at End of Year	**17,711**	18,130	18,121	14,284	14,447	12,678

Management's Discussion and Analysis of the Summary of Operations

The following factors have had a significant effect on the results of the Company's operations during the years 1979 and 1978.

Operating revenues

The increases in operating revenues for 1979 and 1978 were attributable to the following factors (in Million $):

	Electric Revenues		Gas Revenues	
	1979	1978	**1979**	1978
Sales to other utilities	**$ 6.9**	$ 9.1	Not applicable	
Sales to consumers—				
Due to fuel and purchased gas adjustments, respectively	**3.3**	1.4	**$ 5.3**	$ 2.4
Due to sales increases	**.4**	2.2	**3.5**	3.8
Recognition of unbilled revenues and other	**—**	.6	**—**	1.1
Total increases	**$10.6**	$13.3	**$ 8.8**	$ 7.3

Electric sales to consumers increased 0.6 percent in 1979 and 4.1 percent in 1978, while gas sales to consumers rose 7.7 percent and 9.7 percent, respectively. Revenues from sales to other utilities amounted to $22.4 million in 1979 and $15.5 million in 1978.

Fuel used for electric generation, purchased power, and natural gas purchased for resale

The increased costs of fuel used for electric generation and purchased power and of gas purchased for resale, resulted from the following factors (in Million $):

	Fuel for Generation and Purchased Power		Gas Purchased	
	1979	1978	**1979**	1978
Due to changes in Kwh generated and purchased and in Mcf purchased	**$ 3.6***	$ 3.0*	**$ 2.1**	$ 3.2
Due to unit cost increases	**4.5**	4.1	**6.1**	2.8
Total increases	**$ 8.1**	$ 7.1	**$ 8.2**	$ 6.0

*Reflects the commercial operation of Columbia II on April 30, 1978.

Other operations and maintenance

The 1979 increase was primarily due to the commercial operation of the Columbia II plant for a full year. Both years reflected higher labor and material costs, as well as costs associated with serving additional customers.

Depreciation and amortization

A normal reduction of the income tax effects of certain liberalized depreciation allowances permitted for tax purposes in 1979 was more than offset by an increase in straight-line depreciation due to system additions. The 1978 increase in depreciation resulted from additional facilities in service, including Columbia II, and the income tax effects of liberalized depreciation allowances.

Income taxes and investment tax credits

The 1979 increase in current federal income taxes reflects increases in revenues (see "Operating revenues") and reduced investment tax credits, which more than offset the effect of the reduction in the corporate federal income tax rate. Federal income taxes decreased in 1978 essentially because of decreases in taxable income as a result of depreciation on Columbia II and increases in investment tax credits resulting from asset additions.

State income taxes increased in both years due to reductions in the accelerated write-off of pollution abatement facilities.

Property, payroll, and other taxes

Taxes other than income taxes decreased in 1979 primarily due to lower ad valorem (property) tax assessments. Higher tax assessments were the major cause for the increase in taxes other than income taxes in 1978.

Other income

The 1978 change in other income essentially reflected that of the allowance for funds used during construction (AFC) which was affected by the amounts of construction work in progress (Note 1c).

Interest expense

Changes in interest expense reflected fluctuations in debt securities outstanding (Notes 3 and 5), and amounts of construction work in progress subject to AFC.

Common Stock Price Range and Dividends

The range of bid and asked prices of the Company's common stock, which is traded in the over-the-counter market, and the dividends paid for the years 1979 and 1978 are as follows:

	Bid		Asked		Dividends
	High	Low	High	Low	Paid
1979					
First Quarter	16⅜	15½	16⅞	16	37¢
Second Quarter	15⅞	14¼	16⅜	14¾	37¢
Third Quarter	15⅞	14¾	16⅜	15¼	37¢
Fourth Quarter	14⅞	13⅛	15⅜	13⅝	37¢

	Bid		Asked		Dividends
	High	Low	High	Low	Paid
1978					
First Quarter	17	16⅛	17½	16⅝	35¢
Second Quarter	16¼	15⅜	16¾	15⅞	35¢
Third Quarter	16¾	15⅜	17¼	15⅞	37¢
Fourth Quarter	16⅜	15½	16⅞	16	37¢

Electric and Gas Service

Electric

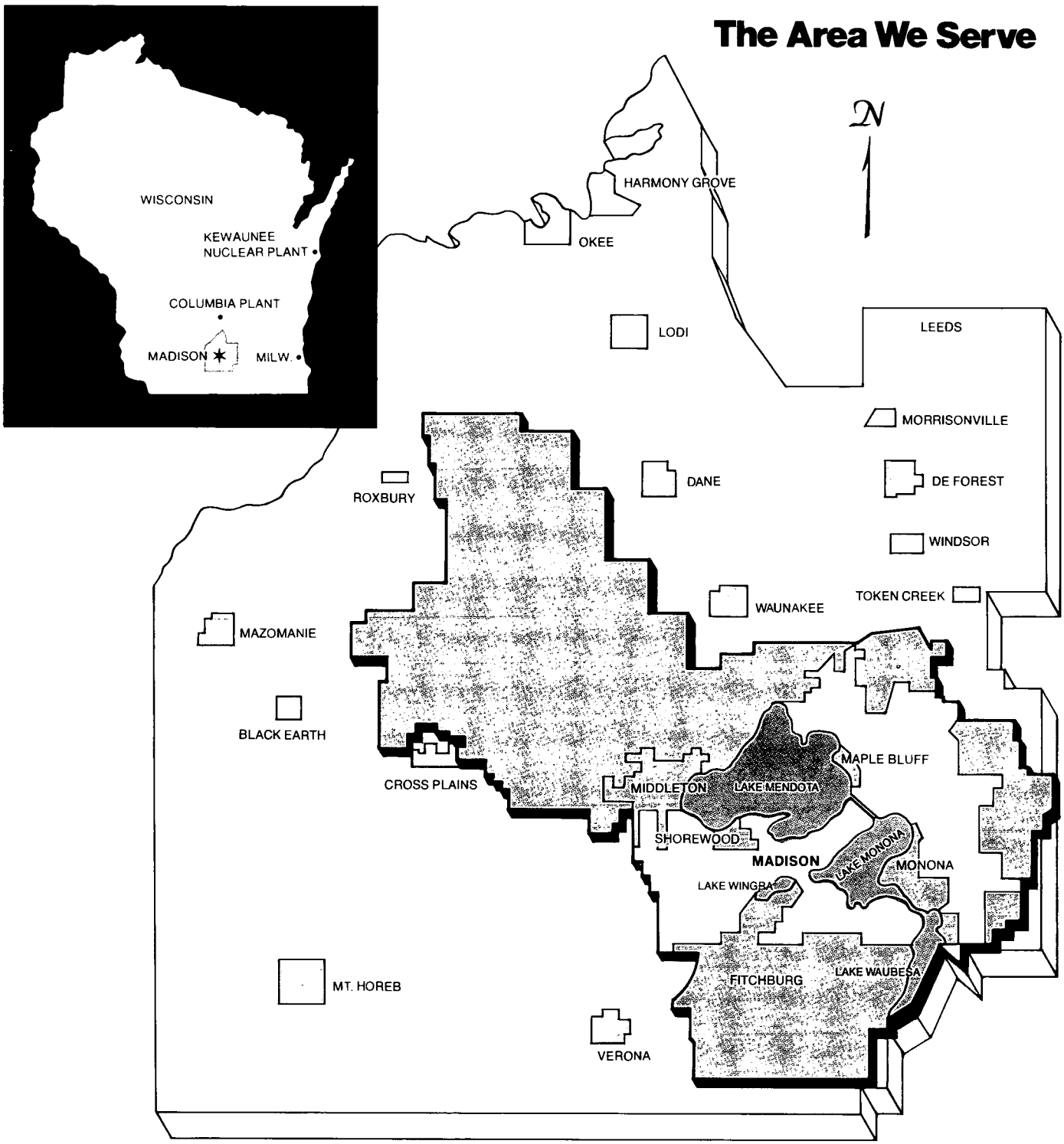
	1979	1978	1977	1976	1975	1974
Sales in Megawatt Hours						
Residential	485,745	503,767	492,397	485,951	486,362	458,638
Commercial Power & Lighting	789,811	766,355	724,977	691,947	671,200	603,792
Industrial Power & Lighting	124,854	114,311	104,743	100,219	102,705	144,244
Street & Highway Lighting & Public Authorities	209,115	215,069	214,769	217,662	214,775	184,041
Other Utilities	690,656	537,616	189,494	148,134	129,132	128,843
Total	2,300,181	2,137,118	1,726,380	1,643,913	1,604,174	1,519,558
Revenue (000)						
Residential	$22,429	$22,130	$20,974	$17,585	$16,393	$12,116
Commercial Power & Lighting	32,739	30,157	27,802	23,043	20,800	14,771
Industrial Power & Lighting	4,547	3,983	3,598	2,905	2,765	2,707
Street & Highway Lighting & Public Authorities	6,704	6,447	6,223	5,176	4,606	2,917
Other Utilities	22,383	15,488	6,426	3,950	2,716	2,867
Total	$88,802	$78,205	$65,023	$52,659	$47,280	$35,378
Customers Served at End of Year						
Residential	83,264	81,671	79,788	78,042	76,404	74,976
Commerical Power & Lighting	11,808	11,609	11,228	11,061	10,804	10,478
Industrial Power & Lighting	122	139	127	141	137	190
Street & Highway Lighting & Public Authorities	40	36	38	35	37	37
Other Utilities	3	3	3	3	3	3
Total	95,237	93,458	91,184	89,282	87,385	85,684

Gas

	1979	1978	1977	1976	1975	1974
Sales in Thousands of Therms						
Residential	68,599	68,145	64,562	66,709	62,309	60,718
Commercial	90,953	88,929	79,433	88,639	90,736	87,714
Interruptible Boiler Fuel	17,354	5,134	5,445	14,929	20,584	17,545
Industrial	15,844	16,302	14,194	15,259	14,831	15,178
Total	192,750	178,510	163,634	185,536	188,460	181,155
Revenne (000)						
Residential	$21,677	$19,135	$16,856	$14,494	$10,908	$9,279
Commercial	24,994	22,134	18,345	16,186	12,573	10,047
Interruptible Boiler Fuel	4,200	1,026	920	1,795	1,950	1,226
Industrial	4,002	3,802	3,006	2,479	1,713	1,312
Total	$54,873	$46,097	$39,127	$34,954	$27,144	$21,864
Customers Served at End of Year						
Residential	54,822	52,574	50,655	48,709	47,000	45,497
Commercial	8,566	8,338	8,016	7,854	7,546	7,281
Interruptible Boiler Fuel	5	4	3	3	5	5
Industrial	73	73	78	65	63	36
Total	63,466	60,989	58,752	56,631	54,614	52,819

Electric Averages	1979	1978	1977	1976	1975	1974
Kilowatt-hours per residential customer—average	5,897	6,241	6,262	6,299	6,455	6,187
Average rate per kilowatt-hour—residential	4.62¢	4.39¢	4.26¢	3.62¢	3.37¢	2.64¢
Gas Averages						
Therms per residential space heating customer—average	1,471	1,527	1,524	1,652	1,616	1,652
Average rate per therm—residential space heating	31.3¢	27.8¢	25.8¢	21.5¢	17.3¢	15.0¢

The Area We Serve



Consolidated Statement of Income

For the years ended December 31, 1979 and 1978

	1979	1978
Operating Revenues (Notes 1f & 7):		
Electric	**$ 89,210,891**	$ 78,588,601
Gas	**55,168,999**	46,389,975
	144,379,890	124,978,576
Operating Expenses:		
Fuel used for electric generation	**31,760,588**	23,027,520
Purchased power	**766,442**	1,349,618
Natural gas purchased for resale	**39,702,101**	31,480,416
Other operations	**15,159,627**	12,925,748
Maintenance (Note 1e)	**5,096,175**	4,383,928
Depreciation and amortization (Notes 1d, 2 & 6)—		
Straight-line depreciation and amortization	**11,628,954**	10,495,666
Additional depreciation (equivalent to estimated reduction in income taxes)	**3,768,763**	4,831,989
Taxes (Note 1i)—		
Current federal income	**7,562,160**	4,055,805
Investment tax credit deferred	**1,681,826**	4,469,720
Investment tax credit restored (credit)	**(671,155)**	(536,946)
Current state income	**1,773,856**	1,183,546
Property, payroll, and other	**5,422,117**	5,923,158
	123,651,454	103,590,168
Net Operating Income	**20,728,436**	21,388,408
Other Income:		
Allowance for other than borrowed funds used during construction (Note 1c)	**—**	29,308
Other, net	**299,558**	246,920
	299,558	276,228
Income Before Interest Expense	**21,027,994**	21,664,636
Interest Expense:		
Interest on long-term debt	**8,018,671**	8,179,390
Other interest	**186,832**	412,277
Allowance for borrowed funds used during construction (credit) (Note 1c)	**—**	(286,513)
	8,205,503	8,305,154
Net Income	**12,822,491**	13,359,482
Preferred Stock Cash Dividend Requirements (Note 3b)	**3,194,401**	2,801,756
Earnings on Common Stock	**$ 9,628,090**	$ 10,557,726
Earnings Per Share of Common Stock (Based on 5,477,541 and 5,376,758 average shares outstanding, respectively)	**$1.76**	$1.96

Consolidated Statement of Retained Income

For the years ended December 31, 1979 and 1978

	1979	1978
Balance Beginning of Year	**$ 23,521,863**	$ 20,865,200
Add—Net income	**12,822,491**	13,359,482
	36,344,354	34,224,682
Deduct:		
Cash dividends on common stock	**8,107,004**	7,742,421
Preferred stock cash dividend requirements	**3,194,401**	2,801,756
Expense of issuing common stock	**47,392**	91,494
Expense of issuing preferred stock	**—**	67,148
	11,348,797	10,702,819
Balance End of Year	**$ 24,995,557**	$ 23,521,863

The accompanying notes are an integral part of the above statements.

Consolidated Balance Sheet

December 31, 1979 and 1978

	1979	1978
Assets		
Utility Plant, at original cost (Note 1a):		
In service—		
Electric (Note 1b)	**$257,331,153**	$249,503,288
Gas	**80,334,821**	74,124,969
	337,665,974	323,628,257
Less—Accumulated provision for depreciation (Note 1d)	**(110,543,911)**	(96,668,826)
	227,122,063	226,959,431
Construction work in progress (Note 1b)	**8,570,359**	6,758,424
Nuclear fuel, net (Note 1g)	**7,576,915**	6,720,039
Total utility plant	**243,269,337**	240,437,894
Investments:		
Investment in future nuclear fuel (Note 1k)	**2,561,109**	2,253,835
Pollution control construction fund	**484,331**	440,670
	3,045,440	2,694,505
Current Assets:		
Cash	**1,756,695**	1,882,025
Deposits for jointly owned electric power production facilities	**1,556,868**	1,462,349
Temporary cash investments, at cost, which approximates market	**1,310,000**	—
Accounts receivable, less reserves of $216,741 and $179,773, respectively	**13,888,337**	13,708,214
Unbilled revenue (Note 1f)	**5,738,385**	6,042,981
Materials and supplies, at average cost	**4,106,184**	3,677,366
Fossil fuel, at cost (Note 1h)	**6,179,185**	2,298,686
Prepayments	**495,302**	431,919
	35,030,956	29,503,540
Deferred Charges (Notes 2 & 6)	**4,642,224**	5,456,188
	$285,987,957	$278,092,127
Capitalization and Liabilities		
Capitalization (see statement)(Note 3):		
Common shareholders' investment—		
Common stock	**$ 44,489,408**	$ 43,518,928
Amount received in excess of par value	**29,262,280**	28,381,680
Retained income	**24,995,557**	23,521,863
	98,747,245	95,422,471
Redeemable preferred stock	**32,825,000**	33,350,000
Long-term debt	**99,229,218**	100,342,422
Total capitalization	**230,801,463**	229,114,893
Current Liabilities:		
Preferred stock sinking fund requirements (Note 3b)	**525,000**	525,000
Maturity of 1979 Series bonds	**—**	1,821,000
Interim loans—commercial paper (Note 5)	**3,900,000**	2,000,000
	4,425,000	4,346,000
Accounts payable	**14,954,360**	12,974,784
Accrued interest	**1,449,505**	1,478,024
Accrued taxes	**5,128,110**	1,813,280
Other	**665,298**	651,221
	26,622,273	21,263,309
Other Credits:		
Contributions in aid of construction	**8,211,054**	5,843,176
Investment tax credit deferred (Note 1i)	**14,367,915**	13,562,704
Unamortized unbilled revenue (Note 1f)	**4,111,252**	4,625,152
Other (Note 6)	**1,874,000**	3,682,893
	28,564,221	27,713,925
Construction Commitments (Note 4)		
	$285,987,957	$278,092,127

The accompanying notes are an integral part of the above statement.

Consolidated Statement of Capitalization

December 31, 1979 and 1978

	1979	1978
Common Shareholders' Investment (Note 3a):		
Common stock—Par value $8 per share—Authorized 6,000,000 shares Outstanding 5,561,176 and 5,439,866 shares, respectively	**$ 44,489,408**	$ 43,518,928
Amount received in excess of par value	**29,262,280**	28,381,680
Retained income	**24,995,557**	23,521,863
Total common shareholders' investment	**98,747,245**	95,422,471
Redeemable Preferred Stock, cumulative, $25 par value, authorized 1,634,000 and 1,655,000 shares, respectively; exclusive of current sinking fund requirements (Note 3b):		
Series A, 9⅜%, 164,000 and 170,000 shares outstanding, respectively	**4,100,000**	4,250,000
Series B, 7.80%, 176,000 and 182,000 shares outstanding, respectively	**4,400,000**	4,550,000
Series C, 7.90%, 273,000 and 282,000 shares outstanding, respectively	**6,825,000**	7,050,000
Series D, 12%, 400,000 shares outstanding	**10,000,000**	10,000,000
Series E, 8.70%, 300,000 shares outstanding	**7,500,000**	7,500,000
Total preferred stock	**32,825,000**	33,350,000
First Mortgage Bonds (Note 3c):		
2⅝%, 1979 series	**—**	1,821,000
4⅝%, 1988 series	**7,526,000**	7,574,000
4¾%, 1991 series	**4,585,000**	4,835,000
5.45%, 1996 series	**8,000,000**	8,000,000
8%, 1999 series	**11,683,000**	11,731,000
7¾%, 2001 series	**14,183,000**	14,195,000
9¾%, 2004 series	**19,430,000**	19,790,000
9¾%, 2005 series	**24,427,000**	24,750,000
6½%, 2006 series	**8,780,000**	8,780,000
	98,614,000	101,476,000
Maturity of 1979 Series bonds	**—**	(1,821,000)
Unamortized discount and premium on bonds, net	**(192,188)**	(200,806)
Total first mortgage bonds	**98,421,812**	99,454,194
Other Long-Term Debt (Note 3d)	**807,406**	888,228
Total long-term debt	**99,229,218**	100,342,422
Total capitalization	**$230,801,463**	$229,114,893

The accompanying notes are an integral part of the above statement.

Consolidated Statement of Sources of Funds Used for Construction

For the years ended December 31, 1979 and 1978

	1979	1978
Funds Generated Internally:		
Net income	**$ 12,822,491**	$ 13,359,482
Items not affecting current sources and uses of funds –		
Depreciation and amortization	**15,397,717**	15,327,655
Amortization of nuclear fuel	**3,042,415**	2,562,368
Investment tax credit deferred – net	**1,010,671**	3,932,774
Amortization of January 1, 1978, unbilled revenue	**(513,900)**	(513,900)
Equity component of the allowance for funds used during construction (Note 1c)	**–**	(29,308)
Other	**271,642**	163,338
Funds provided from operations	**32,031,036**	34,802,409
Less –		
Cash dividends on common and preferred stock	**11,301,405**	10,544,177
Bond sinking fund retirements (including 1979 maturity) and other long-term debt repayments	**2,942,822**	1,445,722
Preferred stock sinking fund retirements	**525,000**	525,000
Net funds generated internally	**17,261,809**	22,287,510
Funds Obtained from Outside Financing:		
Withdrawal from (increase in) pollution control construction fund	**(43,661)**	817,889
Retirement of other long-term debt	**–**	(1,300,000)
Sale of common stock, less expense of issuance	**1,803,688**	1,408,087
Sale of preferred stock, less expense of issuance	**–**	7,432,852
Increase (decrease) in interim loans	**1,900,000**	(1,000,000)
Net funds obtained from outside financing	**3,660,027**	7,358,828
Decreases (Increases) in Other Net Current Assets (exclusive of interim loans and sinking fund requirements):		
Accounts receivable – net	**(180,123)**	(3,124,603)
Unbilled revenue	**304,596**	(903,929)*
Fossil fuel	**(3,880,499)**	817,557
Accrued taxes	**3,314,830**	(3,553,101)
Other, net	**193,744**	495,485
Net (increase)	**(247,452)**	(6,268,591)
Other – Net (includes equity component of allowance for funds used during construction)	**340,483**	2,883,578
Total Funds Used for Construction Expenditures and Nuclear Fuel	**$ 21,014,867**	$ 26,261,325

*Net of $5,139,052 unbilled revenue recorded January 1, 1978.

The accompanying notes are an integral part of the above statement.

Auditors' Report

To the Shareholders and Board of Directors,
Madison Gas and Electric Company:

We have examined the consolidated balance sheet and statement of capitalization of MADISON GAS AND ELECTRIC COMPANY (a Wisconsin corporation) and subsidiaries as of December 31, 1979, and December 31, 1978, and the related consolidated statements of income, retained income and sources of funds used for construction for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Madison Gas and Electric Company and subsidiaries as of December 31, 1979, and December 31, 1978, and the results of their operations and their sources of funds used for construction for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

ARTHUR ANDERSEN & CO.

Chicago, Illinois,
February 20, 1980.

Notes to Consolidated Financial Statements

December 31, 1979 and 1978

1. Summary of Significant Accounting Policies

The consolidated financial statements reflect the application of certain accounting policies described in this note.

a. Utility plant

Utility plant is stated at the original cost of construction, which includes indirect costs consisting of payroll taxes, pensions and other fringe benefits, administrative and general costs, and an allowance for funds used during construction.

Substantially all of the Company's utility plant is subject to a first mortgage lien.

b. Joint plant ownership

The Company and two other Wisconsin utilities, Wisconsin Power and Light Company (WPL) and Wisconsin Public Service Corporation (WPSC), jointly own two electric generating facilities, which account for 54 percent (325 mw) of the Company's net generating capability. Power from the facilities is shared in proportion to the companies' ownership interests. The Company's interests are 22 percent (232 mw) of the Columbia Energy Center and 17.8 percent (93 mw) of the Kewaunee Nuclear Plant. Each company provides its own financing and reflects the respective portion of facilities and operating costs in its financial statements. The Company's portions of these facilities were included in its utility plant in service as follows:

	December 31,	
	1979	1978
Columbia	**$ 75,960,000**	$ 73,065,000
Kewaunee	**38,719,000**	38,066,000
Total	**$114,679,000**	$111,131,000

Expenditures for projects at Columbia and Kewaunee amounted to $575,147 and $1,624,707 at December 31, 1979 and 1978, respectively, and are included in construction work in progress as of those dates.

c. Allowance for funds used during construction

The allowance for funds used during construction (Allowance) is recognized as a cost of utility plant because it constitutes an actual cost of construction and, under established regulatory rate practices, the Company is entitled to earn a fair return on such cost through utility rates. Pursuant to rate orders issued by the Public Service Commission of Wisconsin (the PSCW) since 1974, the Company capitalizes the Allowance (at 7 percent) only on that portion of construction work in progress which exceeds 10 percent of average net investment rate base for the respective calendar year. The annual revenue increase provided for in such orders, including the February, 1980, order (Note 7), has included compensation for the reduction in the Allowance attributable to this revised computation.

d. Depreciation

Depreciation expense includes, in addition to provisions at composite straight-line rates, amounts equivalent to the estimated reduction in income taxes (federal—$3,522,000 and $4,463,000 and state—$247,000 and $369,000 for the years 1979 and 1978, respectively), due to the use of liberalized depreciation allowances permitted for income tax purposes. Such accumulated additional depreciation totaled $29,963,000 and $26,196,000 as of December 31, 1979 and 1978, respectively. Provisions at composite straight-line depreciation rates, excluding the additional depreciation, approximate the following percentages of the cost of depreciable property for each of the years 1979 and 1978: electric, 3.4 percent and 3.5 percent; gas, 3.2 percent and 3.1 percent. These rates are approved by the PSCW and are generally based on the estimated economic lives of property. The reasonableness of the depreciation rates is frequently reviewed by the Company.

The Company's portion of the estimated costs of decommissioning Kewaunee is $6,507,000, which is being recovered through depreciation rates.

e. Property additions, maintenance, and retirements

Normal repairs and the costs of minor items of property are charged to maintenance; whereas, the cost of replacements and betterments of units of property is charged to utility plant accounts. Property units retired or otherwise disposed of in the normal course of business are charged to the accumulated provision for depreciation, and salvage, less removal cost, is credited thereto. No gain or loss is recognized in connection with ordinary retirements of depreciable property.

f. Revenue recognition

In accordance with a PSCW directive, the Company began recording, as of January 1, 1978, unbilled revenue on the basis of service rendered. The directive also provided that the estimated amount of unbilled revenue ($5,139,052) as of January 1, 1978, be recorded as a deferred credit and amortized to income over a ten-year period beginning with 1978. The directive indicates that the amounts amortized are to be deemed reductions of annual revenue requirements in future rate proceedings.

g. Nnclear fuel

The cost of nuclear fuel (Note 1k) is being amortized to fuel expense based on the quantity of heat produced for the generation of electric energy by Kewaunee. Such costs include a provision for estimated future storage and disposal costs of spent nuclear fuel. The tax effect of differences between the fuel cost amortized and that deducted for income tax purposes is included in "Nuclear fuel, net."

h. Fossil fuel

The inventory of fossil fuel is recorded at average cost, except for the Company's Blount Plant coal which is recorded on essentially a last-in, first-out basis. Inventory amounts for Blount coal were $1,297,566 and $421,214 as of December 31, 1979 and 1978, respectively.

i. Income taxes

(1) Depreciation for federal and state income taxes reflects the use of liberalized depreciation allowances permitted for income tax purposes. The estimated reductions in income taxes due to the application of these statutes are provided as additional depreciation as discussed under "Depreciation" (Note 1d).

(2) The investment tax credit is deferred (including the 10 percent basic investment credit and the additional 1½ percent credit relating to the employee stock ownership plan), and the 10 per-

cent deferred amount is amortized over the service lives of the related property.

(3) Certain capitalized indirect costs and certain capitalized research and development costs have been deducted as incurred for federal and state income tax purposes, and the income tax provision is reduced in the year the costs are incurred.

(4) The Company's effective income tax rate, computed by dividing the total of current federal and state income tax expense, net investment tax credit, and additional depreciation by the sum of such expenses and net income, reconciles to the statutory federal income tax rate as follows:

	1979	1978
Effective income tax rate as computed	**52.7%**	51.2%
Restoration of investment tax credit	**2.4**	2.0
State income taxes and state additional depreciation, net	**(4.6)**	(3.7)
Other differences, net	**(4.5)**	(1.5)
Statutory federal income tax rate	**46.0%**	48.0%

j. Rentals

Rentals charged to income, including rentals under noncancellable leases, were less than 1 percent of operating revenues in 1979 and 1978.

k. Subsidiaries

The consolidated financial statements include the accounts of the Company and two wholly owned subsidiary companies which were established for the purposes of holding title to properties to be acquired for future utility plant expansion and holding title to the Company's portion of the nuclear fuel for Kewaunee. All significant inter-company accounts and transactions have been eliminated in consolidation. The Company also has a wholly owned subsidiary established to acquire uranium reserves for Kewaunee and to support the related mining and production operations. The investment in this subsidiary is carried on the equity basis of accounting, and the uranium thus obtained is recorded at cost, including the operations of the subsidiary.

l. Pension plans

The Company has contributory retirement annuity plans for substantially all of its employees. It is the policy of the Company to fund accrued pension costs. As of December 31, 1978 (the date of the most recent actuarial report), unfunded past service costs were $19,000, and the value of assets in the funds was adequate to cover the actuarial value of vested benefits. Past service costs are being amortized over a period of approximately ten years. The provisions for pension costs were $120,000 and $106,000 for 1979 and 1978, respectively; of these amounts, $99,000 and $83,000, respectively, were charged to operating expenses, and the balance was charged to construction and other accounts.

2. Koshkonoug Project

As previously reported, the Company (with a 6.3 percent interest), WPSC, WPL, and Wisconsin Electric Power Company (WE), the designated constructing company, had planned to construct a nuclear facility (Koshkonong) near Fort Atkinson, Wisconsin. In early 1977, the Company ceased making Koshkonong expenditures and withdrew from the project pursuant to a condition of a PSCW rate order. The Company's management has been assured by WE that all expenditures to March 31, 1977, were prudent and reasonable.

Subsequently in 1977, the PSCW (a) approved the request by the other utilities to withdraw their application for Koshkonong, and (b) retained jurisdiction to determine the accounting treatment for the expenditures. The other utilities then applied to the PSCW for a nuclear facility at a site called "Haven." In March, 1979, the PSCW ordered the other utilities to transfer approximately three-fourths of the Koshkonong expenditures to the Haven project capital or deferred charge accounts, and directed the remaining expenditures to be amortized as an operating expense during 1979.

In February, 1980, the other utilities informed the PSCW that they were withdrawing the application for Haven and taking other necessary steps to abandon the project. In a February 14, 1980, order, the PSCW had indicated that, if the other utilities withdrew the application for Haven, these other utilities should amortize as an operating expense substantially all of the expenditures made in connection with the project (including the capitalized Koshkonong expenditures) over a three-year period starting with the completion of their next rate cases, and that the unamortized balance would be included in the capital base for return purposes in rate proceedings. The order also recognized that such expenditures were prudently made.

During 1979, the Company amortized about $521,000 ($284,000 net of income taxes) of its Koshkonong expenditures as an operating expense pursuant to the March, 1979, PSCW order. The remaining portion of the Company's investment ($2,053,773) is being carried as a deferred charge at December 31, 1979. The Company's management believes that the foregoing rate-making treatment will be afforded to substantially all of its deferred Koshkonong expenditures.

continued

3. Capitalization Matters

a. Common stock

The following common stock transactions occurred, and allocations of proceeds were made, as the result of issues pursuant to the Company's Tax Reduction Act Employee Stock Ownership Plan (TRASOP) and its Automatic Dividend Reinvestment and Stock Purchase Plan (Dividend Reinvestment):

	Shares	Common Stock Par Value	Common Stock Excess of Par	Retained Income
1979				
Dividend Reinvestment	**71,674**	**$ 573,392**	**$ 514,535**	
TRASOP	**49,636**	**397,088**	**366,065**	
	121,310	**$ 970,480**	**$ 880,600**	**$ (47,392)***
1978				
Dividend Reinvestment	58,303	$ 466,424	$ 479,813	
TRASOP	33,536	268,288	285,056	
	91,839	$ 734,712	$ 764,869	$ (91,494)*

*Represents expenses of issuing stock.

The Board of Directors has proposed that at the Annual Meeting to be held on April 17, 1980, the shareholders be asked to vote on an amendment to the Restated Articles of Incorporation which would increase the authorized capital stock by an additional 1,000,000 shares of $8 Par Value Common Stock.

b. Preferred stock

During 1978, the Company privately sold 300,000 shares of Series E, 8.70% Cumulative Preferred Stock, $25 Par Value, for $7,500,000 to an institutional investor. The proceeds of the issue were used to repay commercial paper.

The Company, within each 12-month period commencing with the 12-month periods ending as shown below, is obligated to retire a fixed number of shares of each series of preferred stock by redemption, at $25 per share plus accrued dividends, or by purchase at a price not exceeding the optional redemption price then in effect:

	12-Month Period Ending		Number of Shares
Series A	November	1, 1975	6,000
Series B	May	1, 1977	6,000
Series C	November	1, 1978	9,000
Series D	August	1, 1981	26,000*
Series E	August	1, 1984	4,000**

* An additional 26,000 shares may be retired during each of any three 12-month periods commencing after August 1, 1980.

**For the 12-month periods ending August 1, 1994–1998, and August 1, 1999–2008, the Company's annual redemption obligation is 8,000 and 22,000 shares, respectively. The Company may also retire an additional number of shares equal to the annual redemption obligation during any 12-month period ending after August 1, 1984.

Prior to the above dates (except that such date is May 1, 1980, for Series D and August 1, 1983, for Series E), each series of preferred stock may not be redeemed from borrowed funds or proceeds of other preferred stock (i) having interest costs or dividend costs to the Company of less than each series' dividend rate, and (ii) having, in the case of Series E, a weighted average life less than the remaining weighted average life of the Series E stock. Series D may not be redeemed from proceeds of borrowed funds maturing earlier than May 1, 1995, or junior stock.

c. First mortgage bonds

The outstanding $1,821,000 of 2⅝% First Mortgage Bonds due November 1, 1979, were retired at maturity.

The sinking fund requirements of the outstanding first mortgage bonds are $980,000 for each of the years 1980 through 1984. As of December 31, 1979, the Company had satisfied all of its 1980 and $106,000 of its 1981 bond sinking fund requirements.

d. Other long-term debt

In February, 1977, the Small Business Administration made a $1,000,000 loan to the Company in connection with the losses incurred in a 1976 ice storm. The ten-year loan is repayable in equal semi-annual installments (including interest at 6⅝ percent).

4. Constrnction Program

Utility plant construction expenditures for 1980, including the Company's proportional share of jointly owned electric power production facilities, are estimated to be $27,879,000 and substantial commitments have been incurred in connection with such expenditures.

5. Notes Payable to Banks, Commercial Paper, and Lines of Credit

Under a Revolving Credit Agreement with five banks, the Company is entitled to borrow and reborrow until August 31, 1980, up to:

a. $16,000,000 from the five banks in the form of 90-day notes which bear interest at the prime rate in effect at one particular bank three days prior to issuance;
b. $15,000,000 of commerical paper promissory notes; and
c. $5,000,000 of short-term borrowings with other banks.

Pursuant to an order of the PSCW, which type of order can be amended upon the request of the Company, 1980 short-term borrowings may not exceed $20,000,000. Unused lines of credit available to support commercial paper exceeded such commercial paper outstanding at December 31, 1979 and 1978. Commercial paper outstanding at December 31, 1979 and 1978, was issued at commercial paper discount rates prevailing at the time of issuance.

The following information relates to notes payable, commercial paper, and lines of credit for the periods indicated:

	1979	1978
As of end of year—		
Weighted average discount rate on commercial paper outstanding	**13.68%**	10.48%
Unused lines of credit	**$20,400,000**	$20,400,000
For the year ended—		
Maximum amount of borrowings	**$ 7,495,000**	$12,200,000
Average amount of borrowings (based on daily outstanding balances)	**$ 905,000**	$ 4,426,000
Weighted average interest rate on borrowings	**14.17%**	7.60%

In connection with certain lines of credit, the Company maintains average compensating balances ranging from 5 percent of the lines to 15 percent of the amounts borrowed. There are no legal restrictions on withdrawal of these funds.

6. Transmission Line Settlement

As previously reported, in 1975 the Company recorded as a deferred charge the loss (net of income tax and salvage effects) related to a transmission line failure. Amortization of the loss as an operating expense over a 60-month period began in December, 1976. The unamortized balance, included in "Deferred Charges," was $783,916 at December 31, 1979.

In August, 1978, the Company received $3,500,000 ($1,687,000 net of income tax) in full settlement of a lawsuit involving certain parties involved in the design, construction, and collapse of the line. The settlement, net of income tax, has been recorded as an "Other Deferred Credit" and will be amortized, net of the loss amortization, in accordance with the February, 1980, rate order (Note 7).

7. Rate Matters

On February 20, 1980, the PSCW authorized a permanent increase in rates (to be effective after March 11, 1980) designed to produce additional annual revenues of $6,000,000 for electric service and $3,000,000 for gas service. The increase is based on a 13 percent rate of return on common stock equity (the same as previously authorized). The order also contains various electric and gas rate-design changes, including lifeline rates based on customers' income levels, changes in gas service extension rules, and a revised fuel adjustment clause as follows.

Pursuant to the February, 1980, rate order, the Company's electric rate schedules are permitted to be adjusted (after notice to the PSCW) from month to month to reflect changes in the costs of fuel and purchased energy. Gas rate schedules may be adjusted from time to time, upon approval by the PSCW, to reflect changes in the cost of purchased gas. In general, both types of such adjustments are effective immediately (at the time of cost changes) and provide for refinements to assure that cost changes are fully reflected. Formerly the fuel and purchased energy adjustment was limited to fossil fuel cost changes and was generally effective 30 days after such changes.

An appeal, pertaining to the 1976 rate order, refiled by an environmental group and its public affairs officer, is still pending in the Dane County Circuit Court. This appeal involves a challenge to the adequacy of the related environmental screening worksheet presented by the PSCW staff. In the opinion of Company management and of its legal counsel, the outcome of this appeal will not have a material effect on the consolidated financial statements.

8. Segments of Bnsiness

The following table presents information pertaining to the Company's segments of business for 1979, 1978, and 1977. The data does not necessarily reflect rate-making treatment. The preceding Notes are an integral part of this footnote.

	1979	1978	1977
OPERATING INFORMATION (Year Ended December 31):		(Thousands of Dollars)	
Electric Operations—			
Operating revenues	**$ 89,211**	$ 78,588	$ 65,256
Revenues from sales to gas utility	**—**	—	—
Total revenues	**89,211**	78,588	65,256
Operating expenses:			
Operation and maintenance	**47,636**	37,140	28,284
Depreciation and amortization, excluding additional depreciation (a)	**9,236**	8,293	6,816
Property, payroll, and other taxes	**4,157**	4,550	3,901
Operating expenses before income taxes	**61,029**	49,983	39,001
Pre-tax operating income	**28,182**	28,605	26,255
Current federal and state income taxes, net investment tax credit deferred, and additional depreciation (a)	**11,306**	11,219	10,425
Net operating income (b)	**$ 16,876**	$ 17,386	$ 15,830
Construction and Nuclear Fuel Expenditures (Electric)	**$ 14,120**	$ 19,715	$ 31,341

continued

	1979	1978	1977
		(Thousands of Dollars)	
Gas Operations—			
Operating revenues	$ 55,169	$ 46,390	$ 39,140
Revenues from sales to electric utility	7,688	1,053	912
Total revenues	62,857	47,443	40,052
Operating expenses:			
Operation and maintenance	52,537	37,080	30,478
Depreciation and amortization, excluding additional depreciation (a)	2,393	2,203	2,399
Property, payroll, and other taxes	1,265	1,373	1,230
Operating expenses before income taxes	56,195	40,656	34,107
Pre-tax operating income	6,662	6,787	5,945
Current federal and state income taxes, net investment tax credit deferred, and additional depreciation (a)	2,810	2,785	2,000
Net operating income	$ 3,852	$ 4,002	$ 3,945
Construction Expenditures (Gas)	$ 6,895	$ 6,546	$ 5,096
INVESTMENT INFORMATION (at December 31):			
Identifiable assets (c)			
Electric	$207,806	$204,999	$195,072
Gas	60,732	57,071	49,966
Assets not allocated (d)	17,450	16,022	17,296
Total assets	$285,988	$278,092	$262,334

(a) Information regarding amounts recorded as additional depreciation in 1979 and 1978 is set forth in Note 1d. For 1977, the additional depreciation recorded is $2,741,000.
(b) Excludes Allowance for Funds Used During Construction ($—0—, $315,821, and $1,641,465, respectively).
(c) Includes allocated common plant and is net of the respective accumulated provisions for depreciation.
(d) Primarily includes cash, temporary cash investments, accounts receivable, prepayments, and a portion of deferred charges.

9. Quarterly Summary of Operations (Unaudited)

The following is a summary of consolidated operations (in thousands of dollars except earnings per common share) for 1979 and 1978:

	1979				1978			
	(Three Months Ended)							
	Mar. 31	June 30	Sep. 30	Dec. 31	Mar. 31	June 30	Sep. 30	Dec. 31
Operating revenues	$46,243	$28,571	$28,254	$41,312	$37,606	$23,761	$27,693	$35,919
Net operating income	6,920	3,867	4,842	5,099	6,686	3,776	5,549	5,377
Net income	4,919	1,904	2,869	3,130	4,693	1,596	3,473	3,597
Earnings on common stock	4,116	1,104	2,071	2,337	4,044	949	2,772	2,793
Earnings per common share*	76¢	20¢	38¢	42¢	76¢	18¢	52¢	52¢

* Because of the mathematical effect of new common stock issues on average shares outstanding during specific periods, the sum of earnings per share of common stock for any four quarterly periods may vary slightly from the earnings per share for the equivalent 12-month period.

The quarterly results of operations within a year are not comparable because of seasonal and other factors.

10. Supplementary Information to Disclose Effects of Changing Prices (Unaudited)

The following supplementary information is supplied in accordance with the requirements of Financial Accounting Standards Board Statement No. 33, "Financial Reporting and Changing Prices," for the purpose of providing certain information about the effects of changing prices. It should be viewed as an estimate of the approximate effect of inflation, rather than as a precise measure.

The supplemental information presented herein is on a constant dollar basis. Constant dollar amounts represent historical costs stated in terms of dollars of equal purchasing power, as measured by the Consumer Price Index for All Urban Consumers.

Statement of Income from Continuing Operations Adjusted for Changing Prices for the Year Ended December 31, 1979

(Thousands of Dollars*)

	Conventional Historical Cost	Constant Dollar Average 1979 Dollars
Operating revenues	$144,380	$144,380
Fuel used for electric generation	28,719	28,719
Natural gas purchased for resale	39,702	39,702
Other operation and maintenance expenses	21,022	21,022
Depreciation	15,398	26,259
Amortization of nuclear fuel	3,042	3,613
Taxes	15,769	15,769
Other income and deductions—net	(300)	(300)
Interest expense	8,206	8,206
	131,558	142,990
Income from continuing operations (excluding reduction to net recoverable amount)	$ 12,822	$ 1,390**
Income (loss) per common share from continuing operations (excluding reduction to net recoverable amount and after dividend requirements on preferred stock)	$1.76	$(.33)
Purchasing power loss related to reduction to net recoverable amount		$(18,512)
Reduction of purchasing power loss through debt financing		15,476
Net (decrease)		$ (3,036)***

* Excluding per-share figures.

** Including the reduction to net recoverable amount, the (loss) from continuing operations, on a constant dollar basis, would have been $(17,122).

*** Net assets at year-end at net recoverable amount would be $232,571 in average 1979 dollars.

Five-Year Comparison of Selected Supplementary Financial Data Adjusted for Effects of Changing Prices

(In Average 1979 Dollars)

	Years Ended December 31,				
	1975	1976	1977	1978	1979
Operating revenues (Thousands of Dollars):					
Historical cost dollars	$ 74,560	$ 87,781	$104,396	$124,979	$144,380
Constant dollars	$100,600	$111,979	$125,103	$139,114	$144,380
General information					
Reduction of purchasing power loss through debt financing (Thousands of Dollars)					$ 15,476
Cash dividends declared per common share:					
Historical cost dollars	$ 1.20	$ 1.23	$ 1.36	$ 1.44	$ 1.48
Constant dollars	$ 1.62	$ 1.57	$ 1.63	$ 1.60	$ 1.48
Market price per common share at year-end:					
Historical cost dollars	$13.00	$15.75	$17.25	$15.88	$13.88
Constant dollars	$17.00	$19.65	$20.16	$17.02	$13.13
Average consumer price index	161.2	170.5	181.5	195.4	217.5 †

† Based on eight months actual and four months estimated.

continued

The current year's provision for depreciation on the constant dollar amounts of utility plant was determined by applying the Company's depreciation rates to the indexed plant amounts.

Fuel inventories, the cost of fuel used for electric generation, and the cost of natural gas purchased for resale have not been restated from their historical cost. Regulation limits the recovery of fuel and purchased gas costs through the operation of adjustment clauses or adjustments in basic rate schedules to historical costs. For this reason, fuel inventories are effectively monetary assets.

Since only historical costs are deductible for income tax purposes, the income tax expense in the historical cost financial statements is not adjusted.

Under the rate-making principles followed by the PSCW, only the historical cost of plant is recoverable in revenues as depreciation. Therefore, the excess of the cost of plant stated in terms of constant dollars over the historical cost of plant is not presently recoverable in rates as depreciation, and is reflected herein as a "reduction to net recoverable amount." Based on past practices, however, the Company believes it will be allowed to earn on the increased historical cost of its facilities when replacement actually occurs.

To reflect properly the economics of rate regulation, the purchasing power loss related to the reduction of net utility plant to net recoverable amount is offset by the reduction of purchasing power loss resulting from debt financing. During a period of inflation, holders of monetary assets, such as cash and receivables, suffer a loss of general purchasing power, while holders of monetary liabilities are able to satisfy the liability with dollars of lower purchasing power. This unrealized gain, or reduction of purchasing power loss, which is primarily attributable to the substantial amount of debt which has been used to finance utility plant, partially offsets the purchasing power loss because depreciation on this plant is limited to the recovery of historical costs.

Reference is made to the Company's Annual Report on Form 10-K to the Securities and Exchange Commission, which will be filed on or before March 30, 1980. In that report, the Company intends to file replacement cost data as filed in previous years. Current cost amounts, as defined in Statement No. 33, as well as the constant dollar amounts shown herein will be provided in the 1980 Form 10-K.

Construction Program

(Thousands of Dollars)

	1980 Estimated Construction Expenditures		Plant Additions (Including Allowance for Funds Used During Construction) 1979		Annual Average 1974–1978	
Electric Department						
Production Plant	$ 4,262	15%	**$ 3,268**	**16%**	$11,694	38%
Transmission Plant	6,002	22	**2,529**	**12**	8,188	26
Distribution Plant	4,594	17	**4,305**	**20**	2,889	9
General Plant	107	—	**23**	—	56	—
Nuclear Fuel	4,995	18	**3,610**	**17**	2,426	8
Total	19,960	72	**13,735**	**65**	25,253	81
Gas Department						
Distribution Plant	6,155	22	**6,505**	**31**	5,617	18
General and Other Plant	15	—	**49**	—	25	—
Total	6,170	22	**6,554**	**31**	5,642	18
Utility Plaut Common to Both Departmeuts	1,749	6	**811**	**4**	377	1
Total	$27,879	100%	**$21,100**	**100%**	$31,272	100%

General Information

Geueral Offices
P.O. Box 1231
Madison, Wisconsin 53701
Telephone 252-7000 Area Code 608

Trausfer Agent
Harris Trust and Savings Bank
111 West Monroe Street
Chicago, Illinois 60603

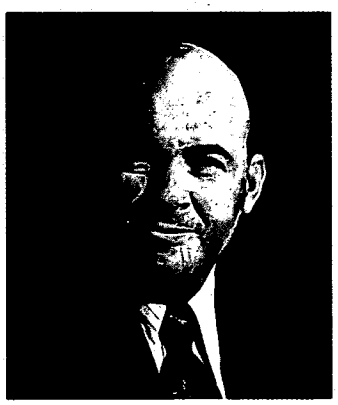
Registrar
The First National Bank of Chicago
One First National Plaza
Chicago, Illinois 60670

Andit Committee
Members of the Audit Committee are: Directors Blaney, Bolz, Gruber, Kubly, Mohs, Sonderegger, and Young.

Annual Meeting
The 1980 annual meeting is scheduled to be held Thursday, April 17, 1980, 7:30 p.m., at the Madison Holiday Inn Southeast located at the Interstate 90–94 and U.S. Highway 12–18 interchange.

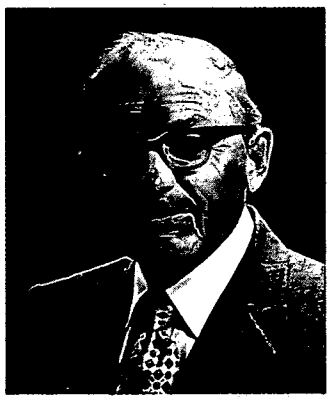
Reports available
Upon written request, the Company will furnish to any shareholder a copy of its 1979 annual report on Form 10-K filed with the Securities and Exchange Commission. Please address requests to G. Howard Phipps, Post Office Box 1231, Madison, Wisconsin 53701.

Board of Directors



Richard E. Blaney
Madison, Wis.
President, Blaney Farms, Inc.
Age 43, Director Since 1974

Robert M. Bolz
Madison, Wis.
Vice Chairman, Oscar Mayer & Co.
Age 57, Director Since 1972



Leo E. Brodzeller
Madison, Wis.
Executive Vice President
Age 62, Director Since 1977

Jon J. Gruber
Middleton, Wis.
President of Gruber Furniture, Inc.
Owner of Gruber Funeral Homes
Age 39, Director Since 1978

Donald J. Helfrecht
Madison, Wis.
President and General Manager
Age 58, Director Since 1972

Stanley V. Kubly
Madison, Wis.
President of Kubly Enterprises, Inc.
Age 71, Director Since 1960

Frederick D. Mackie
Madison, Wis.
Retired Chairman of the Board
Age 69, Director Since 1964

William A. McNamara
Madison, Wis.
Chairman of the Board
Age 71, Director Since 1958

Frederic E. Mohs
Madison, Wis.
Partner, Schlotthauer, Johnson, Mohs, MacDonald & Widder
Attorneys at Law
Age 42, Director Since 1975

John L. Sonderegger
Madison, Wis.
Chairman and Chief Executive Officer–Rennebohm Drug Stores, Inc.
President and Chief Executive Officer–Wisconsin Life Insurance Company
Age 65, Director Since 1971

Louise A. Young
Madison, Wis.
Professor Emeritus, Department of Home Management and Family Living, U.W.–Madison and Financial Consultant
Age 69, Director Since 1973

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